

***United States Court of Appeals
for the
District of Columbia Circuit***



**TRANSCRIPT OF
RECORD**

JOINT APPENDIX

In the United States Court of Appeals
for the District of Columbia Circuit

No. 11,351

680

JESSE M. DONALDSON, Postmaster General of the
United States, and THE UNITED STATES OF
AMERICA on behalf of the Postmaster General,
Petitioners,

v.

CIVIL AERONAUTICS BOARD, *Respondent*

Petition for Review of Order of the Civil Aeronautics Board

United States Court of Appeals
For the
District of Columbia Circuit

FILED JUL 10 1952

Joseph W. Stewart
CLERK

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FOR THE DISTRICT OF COLUMBIA CIRCUIT

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JESSE M. DONALDSON, Postmaster General of the
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and

THE UNITED STATES OF AMERICA, On Behalf of the
Postmaster General, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

Petition for Judicial Review

*To the Honorable, the Judges of the United States Court of
Appeals for the District of Columbia Circuit:*

JESSE M. DONALDSON, Postmaster General of the United States, and THE UNITED STATES OF AMERICA, on Behalf of the Postmaster General, petitioners, respectfully present this petition for judicial review of orders of respondent, Civil Aeronautics Board, and in support thereof represent and allege the following:

I

**THE FACTS AND THE STATUTE UPON WHICH JURISDICTION
IS BASED**

1. This petition is filed pursuant to Section 1006 of the Civil Aeronautics Act of 1938, 52 Stat. 1024, 49 U.S.C. 646. It seeks review of orders of the Civil Aeronautics Board entered in proceedings under Section 406 of the Act, 49 U.S.C. 486, fixing mail pay for Chicago and Southern Air Lines, Inc. (Docket No. 2564, Orders No. E-5793 and E-6045, dated October 18, 1951, and January 18, 1952, respectively). This petition is filed within 60 days after entry of the Board's order of January 18, 1952, denying the Postmaster General's petition for reconsideration. Section 1006; *Braniff Airways v. Civil Aeronautics Board* (1945), 79 U.S. App. D. C. 341, 147 F. 2d 152.

2. The Postmaster General has a substantial interest in the air mail pay orders sought to be reviewed within the meaning of Section 1006 of the Act. He is a statutory party to all airmail pay proceedings before the Board, Sections 406(a) and 406(c), and as such serves as the protector of the public interest in such proceedings. *Seaboard & Western Air Lines v. Civil Aeronautics Board* (1949), 86 U. S. App. 64, 181 F. 2d 515, 518-519, certiorari denied (1950) 339 U. S. 963. The Postmaster General is required to pay air carriers for transporting air mail, out of funds appropriated by Congress for that purpose, at the rates fixed by the Board. Section 406(a). The Postmaster General participated in the proceedings before the Board in which the orders sought to be reviewed were entered, and there urged the objections raised in this petition.

II

THE NATURE OF THE PROCEEDINGS AS TO WHICH REVIEW IS SOUGHT

1. Chicago and Southern Air Lines, Inc. (C. & S.) is a certificated air carrier conducting both domestic and Latin-American operations. Service over the Latin-American routes was inaugurated November 1, 1946. Temporary airmail pay rates for these foreign operations were fixed by the Board by orders dated March 20, 1947 (7 C.A.B. 985) and May 6, 1948 (9 C.A.B. 924).

2. In July 1948, the Board fixed a final subsidy mail pay rate for C. & S.'s domestic operations effective January 1, 1946. 9 C.A.B. 786. The Board estimated that this rate would yield C. & S. a 7.4% return on its investment allocable to domestic operations. Actual operations under this rate, however, have resulted in an average annual return of 12.51% on domestic operations for the years 1948 to 1950. This is \$654,000 more than a 7.4% rate of return would have provided.¹

¹ On October 1, 1951, the Board reopened the current final mail pay rates for the domestic operations of C. & S. and six other domestic trunkline carriers. Order Serial No. E-5747.

3. On May 18, 1951, the Board issued a show cause order proposing final subsidy rates for C. & S.'s Latin-American operations. These proposed rates were retroactive for the period November 1, 1946, to December 15, 1950, and prospective from December 16, 1950. The Postmaster General filed objections to the proposed rates as excessive. He contended, *inter alia*, that the Board was required to offset the carrier's "excess" earnings on its domestic operations in determining the carrier's subsidy "need" on its foreign routes.

The Board, rejecting this contention, issued its opinion and order on October 18, 1951, fixing final mail pay rates, both retroactive and prospective, for C. & S.'s Latin-American operations.² The Board held that Section 406(b) of the Act did not require it "to reduce the carrier's mail pay with any part of [the carrier's] other revenue if there are sound reasons for not doing so as a matter of economic policy."³ The Board, in fixing the rate, determined that the carrier was entitled to a return of 7% for the past period and 10% for the future.

4. The Postmaster General filed a petition for reconsideration, which the Board denied on January 18, 1952. The administrative remedies of the Postmaster General before the Board have now been exhausted.

III

POINTS ON WHICH PETITIONERS INTEND TO RELY

1. Section 406(b) of the Act compels the Board to offset as "other revenue" the excess earnings of the carrier's domestic operations in determining its "need" for subsidy compensation when fixing mail rates for its international operations. The Board is not empowered to refuse

² The opinion and order were based upon a stipulation of facts entered into by the parties to the Latin-American mail pay proceeding.

³ This principle had been enunciated by the Board four months previously in *Western Air Lines, Inc.—Inland Air Lines, Inc., Mail Rates Case*, Order Serial No. E-5467, June 26, 1951. Petitioners are challenging in this Court the validity of that aspect of the Board's order in the *Western* case. *Donaldson, et al. v. Civil Aeronautics Board*, Docket No. 11,259, petition for review filed December 10, 1951.

to offset such excess earnings for reasons of economic policy or otherwise.

2. By failing to offset the excess earnings from the carrier's domestic operations in fixing rates for its international operations, the Board has fixed a rate which produces compensation in excess of the carrier's "need" as provided in the Act, and has allowed the carrier a rate of return in excess of the rate of return previously found reasonable by the Board.

3. The Board exceeded its statutory power or, in the alternative, abused its discretion in failing to offset C. & S.'s "excess" domestic earnings in fixing airmail pay rates on the carrier's Latin-American routes.

IV

THE RELIEF PRAYED

WHEREFORE, petitioners pray that the Board's order be modified to reduce the payments to C. & S. for the transportation of mail on its Latin-American routes by the amount that such payments fail to reflect the carrier's "excess" earnings on its domestic routes, and for such further relief as the Court may deem proper.

(Signed) H. G. Morison
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(Signed) Eugene J. Brahm
 EUGENE J. BRAHM
Chief, Air Mail Section
 Office of the Solicitor

Dated March 18, 1952

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E-5385

UNITED STATES OF AMERICA
 CIVIL AERONAUTICS BOARD
 WASHINGTON, D. C.

Served May 18 1951

Docket No. 2564

CHICAGO AND SOUTHERN AIR LINES, INC.
 Latin American Operations

In the matter of the compensation for the transportation of
 mail by aircraft, the facilities used and useful
 therefor, and the services connected
 therewith.

Adopted: May 18, 1951

Statement of Tentative Findings and Conclusions¹

BY THE BOARD:

This proceeding was instituted by petition filed October 11, 1946, by Chicago and Southern Air Lines, Inc., hereinafter referred to as C & S, for an order fixing and deter-

¹ This statement does not necessarily represent the view of all members with respect to all issues.

mining the fair and reasonable rates of compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, over its Latin American Route.

Informal mail rate conferences² have been held with C&S in order to evaluate past operating results, claimed mail pay and estimates for a future period as submitted by the carrier.

116 In accordance with Section 302.13 of the Procedural Regulations the Board has arrived at the tentative findings and conclusions and has formulated the tentative mail rates set forth herein. Concurrently, the Board is issuing an order directing C&S to show cause why such tentative mail rates should not be established as the final rates in this proceeding.

CERTIFICATE HISTORY

This route was awarded to C&S by the decision of the Board in the *Latin American Case* on May 17, 1946, approved by the President May 22, 1946.³ The route authorized operations between the co-terminal points, Houston and New Orleans, and Havana; from Havana one leg branched to San Juan by way of Camaguey, Port au Prince and Ciudad Trujillo; a second leg extended from Havana to Caracas by way of Kingston, Aruba and Curacao. In January 1947, service to Montego Bay, Jamaica, as an intermediate point between Havana and Kingston was authorized⁴ and in the *Latin American Route Amendment Case*⁵ in March 1949, Camaguey was eliminated and Kingston instead of Havana was made the branching point of the San Juan and Caracas legs.

² Pursuant to Rule 19 of the Board's Procedural Regulations. These conferences were held on January 10-12, 17-19, and 24-26, 1951.

³ Latin American Air Service, 6 CAB 857, 927 (1946).

⁴ Service to Montego Bay, 7 CAB 741, 747 (1947).

⁵ Pan American Airways, et al., Latin American Route Amendment 10 CAB 351, 380 (1949).

The initial petition of C & S filed on October 11, 1946 requested mail pay at the rate of \$1.73 per airplane mile. A subsequent amendment requested that this be increased to \$2.17. A temporary rate of 95 cents per airplane mile was set on March 20, 1947⁶ for the New Orleans-Havana segment.

On March 30, 1948, C & S filed a new petition requesting a rate of \$1.28 per airplane mile for performing the service between Houston-New Orleans and Caracas via Havana and Kingston, and on May 6, 1948 the Board authorized mail pay at the rate of \$1.25 for this service.⁷ This latter rate has been continued until the present time.

PERIODS FOR WHICH RATES WILL BE FIXED

Service from New Orleans to Havana was inaugurated on November 1, 1946. Service from Houston to Caracas via Havana and Kingston began August 1, 1948. The carrier has never begun operations to Aruba, Curacao and Montego Bay nor from Kingston to San Juan.

Service was begun with 50-passenger DC-4's. Constellation aircraft were introduced on December 16, 1950. This four-engine service was supplemented by DC-3 operations between New Orleans and Houston during the first six months of 1949. DC-3's have been in constant use on this segment since June 1950.

The past period for which mail rates will be fixed will be that from November 1, 1946 through December 15, 118 1950, the time during which the carrier was serving most of its system with DC-4 aircraft. The future period will begin December 16, 1950, the date on which service from New Orleans south was offered with Constellation aircraft.

⁶ Chicago and Southern Air Lines, Inc., Latin American Mail Rates, 7 CAB 985 (1947).

⁷ Chicago and Southern Air Lines, Inc., Latin American Mail Rates, 9 CAB 924 (1948).

MAIL RATES FOR THE PAST PERIOD

Scheduled Service Required

The various changes effected by C&S in the pattern of its service over its international system indicate a proper concern on the part of the carrier to develop to the utmost the traffic potentialities existing on its route. The carrier's experimental efforts in this direction, at least up through June 1949, were rewarded with a continually increasing system passenger load factor. The following table sets forth the quarterly available seat-miles, passenger-miles and load factor attained by the carrier on its international system.

CHICAGO AND SOUTHERN'S INTERNATIONAL SYSTEM
QUARTERLY TRAFFIC DATA UP TO JUNE 30, 1949

Quarter Ended	Revenue Passenger Miles (000)	Standard Available Seat-Miles* (000)	Revenue Passenger Load Factor (%)
March 31, 1947	1,773	4,819	36.79
June 30, 1947	1,297	5,244	24.73
Sept. 30, 1947	1,881	5,365	35.06
Dec. 31, 1947	1,747	5,305	32.93
March 31, 1948	1,993	5,365	37.15
June 30, 1948	1,927	5,455	35.33
Sept. 30, 1948**	4,158	10,680	38.93
Dec. 31, 1948	5,118	13,957	36.67
March 31, 1949	6,117	15,087	40.54
June 30, 1949	6,954	16,276	42.73

* DC-3 @ 21 available seats; DC-4 @ 44 seats.

** Service to Caracas inaugurated August 1, 1948.

119 During this period, as indicated, the carrier's load factors steadily improved concurrently with an increase in volume of service operated.

This period of load factor improvement accompanying an increase in capacity not only indicates the success of the carrier's experiments with different types of schedule patterns, but also justified in part at least the carrier's further experimentation with its schedules. Unfortunately, after June of 1949, such experimentation did not meet with

an equal degree of success. The following table indicates that continued schedule changes by the carrier resulted in the operation of substantial amounts of excessive capacity, with a corresponding drop in load factor.

CHICAGO & SOUTHERN INTERNATIONAL SYSTEM
QUARTERLY TRAFFIC DATA 1949 AND 1950

Quarter Ended	Revenue Passenger Miles (000)	Standard Available Seat-Miles* (000)	Revenue Passenger Load Factor (%)
3/31/49	6,117	15,087	40.54
6/30/49	6,954	16,276	42.73
9/30/49	7,832	24,220	32.34
12/31/49	6,424	24,109	26.65
3/31/50	7,100	23,514	30.19
6/30/50	6,882	21,294	32.32
9/30/50	7,362	17,773	41.42

* DC-3 @ 21 available seats; DC-4 @ 44 seats.

The drop in revenue passenger load factor which occurred in the third quarter of 1949 followed a substantial schedule change effected by the carrier on June 27, 1949, when three weekly round trips were added between Houston and Caracas via New Orleans and Kingston. The resulting pattern of service represented a substantially greater volume of revenue plane miles or available seat miles than that offered by C & S at any time to that date. The carrier claims that this increase in service volume was justified on the grounds that its load factor was steadily increasing up until the end of June 1949, that competitive services of other airlines, both foreign and United States Flag carriers, to and from Caracas were improving steadily during this period and that it had no foreknowledge that Venezuelan air traffic volumes would decline markedly from the end of June 1949 forward.

An examination of the facts indicates that while there is some merit to the carrier's position, no real justification has been established for the 75% increase in capacity scheduled to and from Caracas after June 1949. Although load factors between Kingston and Caracas had increased some eight percentage points from the first to the second

quarter of 1949, the load factor for the latter quarter was only 39.8%, a level which hardly justified a substantial increase in the volume of service rendered. While it appears that competitive services existed for Caracas traffic, it has not been shown that such competition was greatly intensified during the summer of 1949; and C&S's increasing load factor on the Kingston-Caracas segment prior to June 1949 would seem to have augured well for its continuing to obtain a reasonable share of the Caracas traffic. It should be noted, finally, that the carrier is restricted from transporting local traffic between Caracas and Havana by the Venezuelan government except on three weekly round trips, a fact which it knew would limit its loads on the added frequencies.

We have stated in other mail rate cases⁸ our concern over the tendency, on the part of some of the carriers, to add schedules on part or all of their systems without having a reasonable expectation that such greater service volumes would result in added revenue greater than
 121 added expenses. Such a policy on the part of the carriers can only result in increases in break-even need and need for mail pay support. Similar results are inevitable where, as here, a carrier adds substantial service volume and fails to reduce it after seeing that the anticipated changes in the balance of revenues and expenses have not materialized. Since we do not propose to underwrite such excessive volumes of service with mail pay, nor to encourage management philosophy underlying such operation, we are impelled to disallow for mail rate purposes a substantial amount of the mileage operated by C&S during the past period.

As already noted, the service operated by the carrier was clearly excessive beginning in the third quarter of 1949. Relatively low load factors continued during the next three quarters, but this condition was rectified on May 29, 1950, when the carrier substantially reduced its service volume.⁹

⁸ Capital Airlines, Inc., Mail Rates, 10 C.A.B. 705, 710 (1949).

⁹ The schedule pattern beginning May 29, 1950, totalled 32,494 miles per week, a reduction of 20% from that operated in the average week during the preceding year.

It is therefore during the approximate 11-month period ended May 29, 1950, that the capacity disallowance will be made.

We do not propose to disallow during this period all of the mileage which now, in retrospect, might be termed excessive. To do so, would, in our judgment, be tantamount to charging C&S management with possession of the gift of infallible prophecy, a responsibility which we do not read into the standard of economic and efficient management laid down in Section 406(b) of the Civil Aeronautics Act of 1938, as being required of the carriers in operations to be underwritten with mail pay.

In determining the specific amount of the disallowance, therefore, we propose to recognize a reasonable period during which the mileage operated will be recognized for mail pay purposes. The purpose of such recognition 122 during this period is to allow C & S an experimental period, during which to test its higher service volume. The most productive schedule pattern operated by the carrier up to June 1950 in terms of load factor and load factor trend was that in effect from December 19, 1948 to June 27, 1949 consisting of approximately one and one-half weekly round trips between Houston and Havana, two and one-half between Houston and New Orleans, nine and one-half between New Orleans and Havana and giving service to Kingston and Caracas of four round trips per week. We find that the mileage operated by the carrier in excess of this schedule pattern during the year following June 1949 could be deemed excessive from the standpoint of load factors, traffic and revenues realized; but that in order to allow for a reasonable period of experimentation, only one-half of such excess will be disallowed for rate-making purposes. In effect, this finding recognizes a period of approximately five and one-half months of the mileage as actually operated, since such operation continued for a total of approximately eleven months.

In view of the fact that on May 29, 1950 the carrier evolved a schedule pattern which reduced by some 20 percent the plane miles operated in the average month during

the preceding year we find that the schedule pattern operated from May 29, 1950 through December 15, 1950 should be recognized in its entirety for mail rate purposes.

The effect of this determination is to disallow 341,000 plane miles operated by C & S up through May 28, 1950 and to recognize the plane mileage operated from that date through December 15, 1950. Appendix No. 1 compares the plane miles, standard available seat-miles, and standard available ton-miles actually operated by the carrier up through December 15, 1950 and that which has been recognized consistent with the above determination.

123 As shown in Appendix No. 1, the 341,000 miles disallowed in the past period approximates 12 percent of that operated by the carrier during the period July 1, 1949 to December 15, 1950, or seven percent of the total plane mileage operated during the entire past period through and including December 15, 1950.

Equipment

During the past period through May 28, 1950 C & S operated most of its schedules on its international system with DC-4 aircraft. In this operation the carrier averaged during the period approximately 7.6 hours per day utilization with such equipment. From May 29, 1950 through December 15, 1950 the DC-4 aircraft were utilized approximately 8.2 hours per day as well as DC-3 aircraft having a daily utilization of 8.4 hours. Even after the indicated disallowance has been made for excessive scheduling the adjusted utilization of the equipment was reasonable. We, therefore, find that the aircraft assigned to the carrier's international division were used and useful and will be recognized in their entirety for rate-making purposes.

Operating Results

While the break-even need level of C&S on a unit basis has, since the beginning of its operations, compared unfavorably with that of other carriers having similar type operations or operating in the Latin American area, the trend

in C & S's break-even need was steadily downward through June 1949. Beginning with the year ended December 31, 1949, however, and for each annual period ended with subsequent quarters C & S's break-even need trend on a unit basis was steadily increasing. This trend is shown in the following table:

Year Ended	Per Revenue Ton-Mile	Per Standard Available Ton-Mile*
	Reported Break-Even Need	
12/31/48	40.51¢	13.55¢
3/31/49	36.45	12.58
6/30/49	30.83	11.08
9/30/49	30.58	10.32
12/31/49	33.69	10.49
3/31/50	36.40	10.84
6/30/50	39.74	11.48
9/30/50	36.82	11.58

* DC-3 @ 2.4 tons; DC-4 @ 6 tons.

The relatively high level of the carrier's break-even need is in large part due to the very low traffic potential on its international system particularly that south of Havana. This is shown in Appendix No. 2 which compares the density of C & S's international system with that of seven other carriers and indicates that except for Colonial Airlines and Braniff Airways, C & S's traffic density in terms of revenue ton-miles per route mile per day was the lowest of the entire group.

The fact that the carrier's increasing break-even need after June 1949 was accompanied by relatively low unit operating expenses and declining load factors and yields indicates that revenue factors rather than unduly high operating expenses were responsible. Appendix No. 3 indicates that as the carrier increased its service volume its unit expenses on a comparative basis achieved a very low level, but that in spite of these economies its revenues declined to such an extent that break-even need nevertheless increased.

Revenues

The carrier has substantiated with factual proof its claim that over the entire period of its operations it actively resisted attempts of other carriers to reduce the general level of fares in the Caribbean area. We therefore
 125 find that it has been only as a result of C & S's attempt to meet competitive fares where necessary that its unit revenues have been steadily declining during recent years; and that therefore the level of its unit revenue yields was reasonable during the past period.

The only adjustment to operating revenues is the loss which results from the capacity disallowance previously discussed. We find, in view of the relatively constant degree of competition to which the carrier's traffic was subject, that the load factor attained by it for the year ended June 1949 (prior to the addition of the capacity found to be excessive) was a load factor reasonably attainable during the subsequent year at the same service volume. We have therefore estimated the passenger-mile volume which would have obtained without the addition of the excessive capacity during the year ended June 30, 1950, by applying the prior year's load factor to the capacity operated as of June 1949. The passenger-mile volume carried in excess of that amount is estimated as the volume which would have been lost had the excess capacity not been operated. Adjustments to reported volumes, not only of passenger-miles, but also of freight and excess baggage, are shown in Appendix No. 1.

Passenger, freight and excess baggage revenues during the past period have been reduced by \$133,000, reducing non-mail revenue from \$6,012,000, as reported by the carrier, to \$5,879,000, (Appendix No. 4) which reflects the adjustment outlined above.

Expense Adjustment for Excess Capacity

Appendix No. 4 sets forth the adjustments which have been made to the reported expense figures of C & S. The disallowance of 341,000 plane miles previously indicated

as the excessive plane miles operated during the year
 126 ended June 30, 1950 requires a reduction in the carrier's expenses. The reduction in expense in the flying operations and in the direct maintenance categories totals \$209,000 and was determined on the basis of the reported expense per revenue plane mile in these categories for the year ended June 30, 1950. The adjustment required in depreciation expense and in ground and indirect maintenance expense totals \$31,000 and was determined on the basis of the change in allocation of these expenses to the international operation. Ground operations expense as reported was reduced by \$8,000 on the basis of arrivals and departures. Passenger service expense as reported was reduced by \$15,000 on the basis of the cost per passenger-mile for the year ended June 30, 1950. Selling expenses, including traffic and sales, advertising and publicity, were reduced by \$24,000 from the reported figure for the year ended June 30, 1950 on the basis of the percentage by which non-U. S. mail revenues had been reduced from the reported figures for that year. General and administrative expense was reduced by \$26,000, the adjusted figure estimated at 8.92 percent of total adjustments excluding general and administrative expense.

The total of these expense adjustments attributable directly to the elimination of excessive capacity totalled \$313,000. As shown in Appendix No. 4, pages 2 and 3, the net adjustment to recorded break-even need resulting from the elimination of excessive capacity results in a net decrease in break-down need of \$180,000 after the revenue adjustments of \$133,000 are subtracted from the adjustments to expense.

Direct Maintenance

The only adjustment required in the direct maintenance account is to provide for amortization of the built-in overhaul for the DC-4 aircraft and engines, and the amortization of actual overhaul expenses. C & S does not
 127 have overhaul reserves and has charged overhaul costs to direct maintenance expenses as incurred.

In order to avoid cost fluctuations and in accordance with the built-in overhaul adjustments in the depreciation expense, the carrier's overhaul expenses have been reversed and capitalized and their amortization effected by spreading experienced costs over the overhaul cycle. As a result, direct maintenance expenses have been increased by \$66,000.

Depreciation—Flight Equipment

In the C & S domestic rate opinion of July 1, 1948,¹⁰ the Board recognized and capitalized a high level of DC-4 integration costs with the express condition that for purposes of mail pay determination the carrier's DC-4 depreciation expense be computed on a five-year service life rather than four years which was then considered reasonable for other carriers. C & S has not conformed with this requirement and has been depreciating its DC-4 equipment over less than four-year periods, in some cases at a service life as short as fifteen months. In accordance with our previous domestic opinion, adjustments amounting to \$425,000 are made to reflect a service life of five years and ten percent residual value.

The elimination of the built-in overhaul from the depreciable cost of DC-4 aircraft, in accordance with the Board's previous opinions on this matter, results in a decrease in depreciation expenses amounting to \$85,000 for the hulls and \$30,000 for the engines, raising the total adjustment to depreciation expenses to \$540,000.

Allocation Between Domestic and International Services

In the carrier's domestic mail rate proceeding, the revised allocation of certain common expenses between domestic and international operations, which had been
 128 effected by the carrier on January 1, 1948, was applied from the beginning of international operations on November 1, 1946.¹¹ The corresponding adjustments in

¹⁰ Chicago and Southern Air Lines, Inc., Mail Rates, 9 CAB 786, 798 (1948).

¹¹ *Supra*, Note 10.

international operating results for the period from November 1, 1946 to December 31, 1947 are: an increase of \$19,000 in ground and indirect maintenance, an equivalent decrease in advertising and publicity expense and an increase of \$33,000 in general and administrative expense.

DC-4 Integration Costs

Amortization of DC-4 developmental and training costs over a five-year period, which was provided for in the domestic mail rate proceeding, has similarly been recognized. System amortization charges were allocated to international operations in proportion to adjusted depreciation expenses. In view of the sale and retirement of the carrier's DC-4's in the latter half of 1950, amortization was accelerated in the last quarter of 1950 to absorb the remaining balance of integration costs. The amount of \$114,000 claimed by the carrier has been adjusted to eliminate charges prior to the beginning of international operations on November 1, 1946, resulting in a total allowance of \$111,000 for the review period.

Amortization of Preoperating Expense

Preoperating expenses of \$49,000 incurred by the carrier in preparing for certificated operations after the grant of its route certificate have been examined and found reasonable in nature and amount. Accordingly, their complete amortization in the review period has been allowed.

Nonoperating income and expense

Profit on the sale of the carrier's DC-4 aircraft, which were used in international operations during the review period, has been included as other income to reduce break-even need pursuant to Board policy. The profit
 129 has been calculated from the depreciated cost as adjusted to reflect application of the standard five-year life and ten percent residual value for DC-4 equipment, and elimination of "built-in overhaul" from the depreciable cost. The amount of \$19,000 has been allocated as profit to

international operations on the basis of relative depreciation charges to international and domestic operations.

The carrier has claimed \$65,000 for contingent expenses of foreign operations. This has been disallowed in conformance with the Board's established policy that unrealized and purely prospective costs may not be recognized for the purpose of determining mail rates.

Adjusted Break-Even Need

On the basis of the foregoing adjusted total expenses of \$9,001,000 and operating revenues of \$5,879,000, the carrier's break-even need is \$3,122,000 or 67.27 cents per revenue plane mile. This amount is 18.5 percent below the breakeven need of \$3,831,000 claimed by the carrier. After full consideration of the various factors affecting the operations and the break-even need for the period November 1, 1946 to December 15, 1950, we believe that the carrier's revenues and expenses, as herein adjusted, are fair and reasonable for mail pay purposes.

During the past period, 1948-1950, for which the international rate is established herein, the domestic division of C & S was operating under a final mail rate which was made effective January 1, 1948 (*Chicago & Southern Air Lines, Inc., Mail Rates*, 9 C.A.B. 786), and is currently outstanding. Over that period the domestic division earned an average return on investment estimated at 12½ percent. The level of such earnings poses the problem as to

whether any portion of the revenues realized by
 130 C & S under its domestic mail rate can or should
 be offset against the need which would otherwise be found to exist in relation to C & S's international operations, with a resulting reduction in the mail pay to be provided for such operation. We have considered the possible offset of such revenues, but we find that policy considerations to which we advert below render such offset inappropriate.

One primary objective of the Act is to further the development of the airline industry to a point where, in general, it will reach a self-sufficient status. From the mail

rate standpoint this goal is best attainable by placing carriers on permanent rates rather than on cost-plus bases for mail payments. *Transcontinental and Western Air, Inc. v. Civil Aeronautics Board*, 336 U. S. 601 (1949). For it is under permanent rates that there exists maximum incentive on the part of carriers to economical and efficient operation. This conclusion follows because, with the realization that they will retain the advantages of good earnings and yet stand any losses which may eventuate thereunder without reimbursement, carriers will, while on closed final rates, bend every effort to keen, economical, and prudent management.

The responsibility of the Board to place carriers on final future rates as rapidly as possible is an exacting one to discharge even where the carrier operates either
 131 solely in the domestic or solely in the international area. With regard to carriers comprising both domestic and international divisions, the practical problems presented in any attempt to place both divisions on final rates simultaneously are more difficult because many considerations which enter into the fixing of an international rate are different from those entering into the establishment of a domestic rate. As a practical matter, unless a permanent rate under which the carrier will bear the risks of the future can be fixed for domestic operations, where that course is feasible, without the necessity for determining simultaneously the rate for a companion international division, it may often prove to be impossible to fix any permanent rate for the carrier for an extended period of time. Indeed, if we were to determine that such rates must invariably be established simultaneously, it might well turn out to be impossible in some cases to establish future final rates at any time for carriers comprising both domestic and international divisions. Yet, the fixing of forward final rates which stimulate to the maximum the carrier's incentive to low cost operation and high revenue production cannot be foreclosed to the Board if its statutory responsibilities are to be discharged adequately.

132 The public interest in maintaining and furthering the incentive to carriers generated under forward final rates leads us to the conclusion that at this time, without review of any question of power but simply as a matter of policy, we should not offset the profits of the domestic division of C & S earned under the closed rate in establishing the mail rate for the international operation.

We find, therefore, that the principles of the Act will not be best served now by a policy of application of excess earnings under a past rate, as in the case before us, and, accordingly, that the need of the international division of C & S should not be reduced by offset of any portion of the earnings of its domestic division during the three years in issue. In this connection, of course, it should be borne in mind that although the domestic division retains the earnings experienced while on the unconditional permanent rate fixed for that division, we have it in our power, as does the Postmaster General, to institute a proceeding looking toward decrease of the rate for that division when it passes the bounds of reasonableness; and the
133 Board has exercised that power in the past.¹²

Simultaneously with the issuance of this statement, we are causing studies to be made by the staff of the earnings of C & S and of other carriers similarly situated to determine whether proceedings should not be instituted looking toward a decrease in their current final domestic mail rates.

Past Period Investment

Investment claimed by the carrier and recognized for the past period has been set forth in Appendix No. 5, together with adjustments required for rate-making purposes. The average investment claimed by C & S from the beginning of international operations to December 31, 1950
134 amounts to \$1,270,000. This sum does not vary significantly from the investment as herein adjusted, totaling \$1,360,000.

¹² A recent example is the show cause order in Pioneer Air Lines, Inc., Mail Rates, Docket No. 4000, Order Serial No. E-3010, July 14, 1949, which was finalized on September 15, 1950 by Order Serial No. E-4613.

With respect to working capital, the amount of \$508,000 claimed by the carrier has been reduced by \$35,000. In arriving at working capital investment, C&S neglected to consider all working capital components, namely, the prepayments of \$16,000 and deferred charges of \$2,000 among assets, and deferred credits of \$25,000 and operating reserves of \$6,000 among liabilities. These items when properly included effect a net reduction in working capital of \$13,000. A further reduction of \$22,000 has been made to eliminate excess mail pay from working capital as determined in this order. The resulting recognized working capital of \$473,000 is equivalent to almost three months' adjusted cash operating expenses, a level which indicates a satisfactory financial condition.

The built-in overhaul adjustments and the adjustment of DC-4 depreciation which accrued during the review period result in an average increase in the carrier's investment in flight equipment of \$201,000. This amount comprises: (a) \$183,000 arising from the adjustment of DC-4 depreciation expense to reflect the change in service life from four years and ten percent residual value to five years and ten percent residual value; and (b) \$18,000 conforming to the adjustment of operating expense for built-in overhaul costs.

In accordance with the policy of disallowing investment in equipment purchase funds for rate-making purposes, as set forth in previous cases,¹³ the amount of \$154,000, 135 representing the average amount of advance payments for the purchase of Constellation aircraft, has been removed from investment. During the review period C&S did not use the Constellation aircraft for which these funds were established, and therefore no provision for interest has been made in the past period investment.

Prepayments and deferred charges of a current nature amounting to \$18,000 have been transferred from long-term prepayments to the more appropriate category of working capital as discussed above. Additional amounts of \$25,000

¹³ Braniff Airways Mail Rates, 9 C.A.B. 607, 624 (1948);

Pan Am. Airways, Inc., Transatlantic Mail Rates, 8 C.A.B. 267, 285 (1947).

and \$71,000 have been provided herein to reflect the capitalization of preoperating costs and DC-4 integration costs, respectively, in accordance with the amortization of these items allowed in expenses.

After making the foregoing adjustments the investment recognized herein for the past period amounts to \$1,360,000 (Appendix No. 5).

Mail Rate

The break-even need for the review period, as determined on the basis of the foregoing adjustments, is \$3,122,000. In addition to this amount, the fair and reasonable mail rate must include a fair return on recognized investment. It has been the Board's consistent practice to provide a somewhat lower rate of return for past periods than for future periods in view of the fact that for past periods the probability of error in estimates of operating results is removed and operating risks have been realized. Accordingly, a return of seven percent per annum on the recognized investment of \$1,360,000 will be provided in addition to the break-even need for the review period. This return amounts to 136 \$393,000. The allowance for Federal income taxes of \$130,000 has been computed by removing revenue adjustments and deducting expense disallowances from net taxable income in accordance with the provisions of recent mail rate decisions of the Board.¹⁴

On the foregoing basis, we find that the fair and reasonable rate for the transportation of mail by aircraft over the carrier's international routes for the period November 1, 1946 through December 15, 1950, is \$3,645,000, which is equal to 78.51 cents per revenue plane mile. The mail pay of \$3,645,000 is inclusive of and not in addition to the mail compensation heretofore received by the carrier for mail transported from November 1, 1946 to December 15, 1950, inclusive.

¹⁴ Colonial Air Lines, Inc., Bermuda Mail Rates, Order Serial No. E-5065 of January 24, 1951.

Western Air Lines, Inc. and Inland Air Lines, Inc., Mail Rates, Order Serial No. E-4870 of November 24, 1950.

MAIL RATES FOR THE PERIOD ON AND
AFTER DECEMBER 16, 1950

Scheduled Service Required

The carrier estimated that 1,679,000 revenue plane miles would be flown during a future year. This estimate is based upon a daily round trip between Houston and New Orleans with DC-3 aircraft which amounts to an annual total of 219,000 revenue miles, and the daily operation of Constellation equipment over the New Orleans-Havana-Kingston-Caracas segment totaling 1,460,000 annual revenue miles.

On December 16, 1950 the carrier initiated the operation of Constellation equipment on its international routes, substituting this aircraft on all its former DC-4 schedules. As we pointed out in the section related to the past period, the traffic on the segments south of Havana did not justify the maintenance of daily service over this portion of the route after a reasonable experimental period. This situation is aggravated by the use of the larger and more modern
137 equipment which the carrier indicates is necessary for competitive reasons. While we realize that competition is encountered on the Havana-Caracas segment, there appears to be no compelling reason to warrant the recognition of seven weekly round-trips with Constellation aircraft. In particular, the load factors experienced on this segment in the year 1950 in the operation of seven weekly round-trips with DC-4 aircraft, hardly justify continuing these schedules with Constellation equipment.

We find, therefore, that four round trips per week Havana-Kingston-Caracas with Constellation aircraft is a reasonable volume of service on this segment for a future year. The elimination of 413,000 miles applicable to the three additional round trips per week estimated by the carrier results in 1,047,000 revenue miles to be recognized for the Constellation operation. This mileage, added to the 219,000 miles to be flown with DC-3 aircraft, brings the total revenue plane miles to be recognized for a future year to 1,266,000.

On the basis of the revenue miles recognized above and the standard capacities of 21 seats and 2.4 tons for DC-3 aircraft and 52 seats and 8.0 tons for Constellation equipment, the available seat-miles and available ton-miles to be recognized for the future year are 59,043,000 and 8,902,000, respectively (Appendix No. 6).

In view of the competitive routings which exist for passengers traveling from the United States to Kingston and Caracas, it is reasonable to expect that the reduction which we have made in the carrier's service to and from these points will result in a reduction in the carrier's ability to generate traffic. Consequently, the carrier's estimate of 31,100,000 revenue passenger-miles to be carried in the future year has been adjusted to reflect the indicated decrease in the capacity to be recognized. Since we have reduced

the service to be recognized by 3/7ths between Havana and Caracas a reasonable reduction in the passenger traffic estimate for Kingston and Caracas passengers appears to be a decrease of 2/7ths. This estimate of a 2/7ths reduction is necessarily based on judgment since we are unaware of any exact method by which to determine the decline in passenger traffic resulting from a reduction in capacity to be operated. To the extent that the estimated decline is not directly proportional to the curtailment of capacity, it is our view that this is a reasonable estimate since even the recognized capacity after reduction exceeds what might be termed a minimum pattern of service for the Havana-Caracas segment.

The 2/7th reduction in passenger traffic has been applied to all traffic originated or terminated at Kingston and Caracas except for the local Caracas-Havana traffic which can be carried by C&S only on three schedules per week. Applying the 2/7th reduction to the traffic estimated with the single exception noted, we have recognized a decrease of 5,200,000 revenue passenger-miles from the total estimated by the carrier for a future year. This results in a net to be carried by C&S of 25,900,000 revenue passenger-miles and results in a passenger load factor for the future year

of approximately 44 percent for the entire international route.

Freight ton-miles have been estimated at 533,000 on the basis of the freight revenue forecast for the future year and the freight yield per ton-mile estimated by the carrier.

Excess baggage ton-miles and foreign mail ton-miles have been estimated by dividing the estimated revenue in each category by the yield per ton-mile experienced during the third quarter of 1950, which results in 90,000 excess baggage ton-miles and 3,000 foreign mail ton-miles.

The U. S. mail ton-miles have been forecast at 23,000 for the future year by applying the average load experienced during the third quarter of 1950 to the estimated miles to be flown.

139 *Non-U. S. Mail Revenues*

The carrier estimates \$2,411,000 in passenger revenues for a future year as set forth in Appendix No. 7. An adjustment of this amount is necessary to reflect the reduction in passenger-miles attributable to the reduced volume of service which has been found adequate to meet the needs of the traffic.

Since the Kingston and Caracas traffic produce higher passenger yields than realized elsewhere on the carrier's route, it is necessary that the traffic be eliminated on these segments at a yield higher than the average passenger yield of 6.77 cents forecast by the carrier. A yield of 7.50 cents per passenger-mile, representing the estimated average yield of the passenger traffic to Venezuela, was used in determining the passenger revenue lost due to reduction in Caracas traffic, and 7.00 cents per passenger-mile was used for the loss of Kingston traffic. The passenger revenue forecast by the carrier has thus been reduced by \$385,000 leaving an adjusted amount of \$1,720,000 or 6.64 cents per passenger-mile.

The excess baggage revenue of \$74,000 estimated by the carrier has been adjusted to \$60,000 in order to retain the relationship to passenger revenue indicated in the carrier's forecast.

The freight revenue forecast by the carrier is \$205,000 or 12 cents per revenue mile. Applying this yield per revenue mile to the revenue miles estimated for the future results in \$152,000 of freight revenue for the future year.

Foreign mail revenue for a future year which was estimated at \$8,000 by the carrier has been revised to \$7,000, based upon the level of other revenues. The estimate of \$19,000 in other non-U.S. mail revenues forecast by the carrier has been accepted as reasonable.

140 *Total Non-U.S. Mail Revenue*

The total non-U.S. mail revenues, which were estimated by the carrier to be \$2,411,000, have been reduced by \$453,000 to reflect the adjustments in the various categories discussed above. Therefore, the adjusted estimate of total non-U.S. mail revenues is \$1,958,000.

Operating Expenses

We have used the adjusted expenses for the year ended June 30, 1950 as the base year for estimating future expenses, and have made allowances for increased costs which became effective in 1950 but were not fully reflected in the base year. The bases for future year estimates have been detailed by account in Appendix No. 7.

In forecasting flying operations expense for a future year, we have applied the carrier's estimated cost of 28.29 cents per DC-3 revenue plane mile to its projected DC-3 mileage, and its estimated cost of 69.05 cents per revenue plane mile of Constellation operation to the adjusted mileage for this operation. Likewise, DC-3 direct maintenance expense represents application of the carrier's cost estimates of 10.04 cents per revenue plane mile. Direct maintenance expenses of Constellation aircraft have been estimated at 35.00 cents per plane mile. Depreciation claimed by C & S has been adjusted to reflect adoption of the standard 7-year life and 10 percent residual value for Constellation equipment in place of the 5-year life proposed by the carrier. These adjustments effect a reduction of \$575,000

in the carrier's estimated aircraft operating expenses and result in a recognized total of \$1,473,000 for a future year.

The carrier's forecast of ground and indirect expenses has been found reasonable after downward adjustments of three expense categories. Passenger service expense, taken at the carrier's unit cost of 0.926 cent per revenue passenger mile, has been reduced to agree with the adjusted revenue passenger-miles. Traffic and sales and advertising and publicity expense claimed by the carrier has been reduced to an amount aggregating 20 percent of estimated non-U.S. mail revenues, a ratio approximating that established for comparable carriers in recent rate cases; and on the basis of a similar comparison, general and administrative expense has been reduced to an amount representing 10 percent of other cash expenses. These adjustments, totaling \$266,000, result in adjusted ground and indirect expenses of \$1,821,000.

Total operating expense for a future year has thus been found to be \$3,294,000, equivalent to 260.25 cents per revenue plane mile. This is a high level of expense, but represents the summation of costs which have been individually examined and found reasonable, and is 20 percent below the carrier's estimate. As indicated in the foregoing discussion, the high cost is primarily due to the introduction of Constellation aircraft to enable the carrier to maintain its competitive position and to coordinate with Constellation service on its domestic system. The inherently high unit cost of operating this equipment over the international route, with its relatively low traffic density, has been weighed with regard for these factors. The influence of the general rise in material and labor costs being experienced has also been taken into account. After consideration of the particular circumstances of the carrier's situation, the stated amount of its future year operating expenses has been recognized.

Break-Even Need

The adjusted break-even need for the future year based on non-U.S. mail revenues of \$1,958,000 and total expenses of \$3,294,000 is \$1,336,000, equal to \$1.06 per revenue plane mile.

142 *Investment*

The recognized investment allocated to the international operations for the future period is based on the preliminary balance sheet as of December 31, 1950, which has been adjusted to reflect the elimination of amounts not recognized for rate-making purposes. These adjustments have been summarized in Appendix No. 8.

The total future investment claimed by C & S amounts to \$3,044,000. Of this total \$916,000 represents net working capital based upon the carrier's estimate of three months' cash operating expenses. As of December 31, 1950, however, the carrier's working capital allocated to international operations amounted to \$468,000 after the inclusion of \$104,000 representing 26.30 percent of \$397,000 obtained from the sale of two DC-4 aircraft during the first quarter of 1951. The ratio of 26.30 percent which has been used to allocate working capital between domestic and international operations represents the relationship of estimated cash operating expenses for international operations to the total cash operating expenses of the entire C & S system. From the total working capital of \$468,000 we have deducted \$193,000 which is the international portion of the excess mail pay received by C & S during the review period. The net resulting working capital as herein determined for rate purposes amounts to \$275,000.

Since all Constellation equipment is used by C & S on a system basis, the carrier estimates that one-third of the common investment in six Constellation aircraft should be allocated to international operations. This allocation on the basis of revenue plane miles estimated for the future period appears reasonable and is recognized in the future investment. As indicated in Appendix No. 8, the investment in

Constellation equipment, after restoring the book value of the aircraft to the level of December 16, 1950, is 143 \$2,334,000 or one-third of \$7,000,000, the approximate total cost of six Constellations. To this amount is added \$9,000 representing capitalized interest on the equipment purchase funds relative to these aircraft.

Prepaid and deferred items of a current nature, claimed by the carrier as part of its fixed assets have been eliminated and provided for in working capital. Long term operating property prepayments of \$24,000, the same amount reported in 1950, are found reasonable and are so included in future investment. An additional \$83,000 claimed by the carrier for this category of investment does not appear to be adequately supported and is herein disallowed for rate-making purposes. After all adjustments, the net decrease to claimed investment is \$294,000 resulting in recognized investment of \$2,750,000.

Determination of Mail Rates

In accordance with our findings discussed previously herein, we have determined C & S break-even mail pay requirements to be \$1,336,000 equal to \$1.06 per revenue plane mile as forecast. This determination is \$388,000 or 22.51 percent lower than the break-even of \$1,724,000 estimated by the carrier. The acquisition of the Constellation aircraft has expanded the investment base so that application of a ten percent rate of return, which we have consistently considered fair and reasonable for international operations in a future period, produces a return element of \$275,000 equal to 21.72 cents per revenue plane mile. This compares with an average of 8.36 cents per mile recognized in the past period. Provision for federal income taxes at 47 percent results in the amount of \$244,000 equal to 19.27 cents per revenue plane mile. Total mail pay requirements are, therefore, \$1,855,000 or \$1.47 per revenue plane mile flown in scheduled service.

144 The mail pay requirement of C&S for the future is at a higher rate than any of those currently in

effect for other international carriers. It exceeds the requirement of the other carriers by a substantial margin on any of the customary bases of mail pay comparison, such as plane miles, mail ton-miles or as a percentage of total revenue.

As indicated above, this relatively high level of mail pay, brought about by the operation of Constellation aircraft over a route of very low traffic density, is justified by the circumstances peculiar to C&S operation.

The very fact that the rate established for the future period is substantially higher than that found appropriate for the past period necessarily raises the question whether some adjustment of the route pattern and the volume of services provided south of Havana may not be required. We do not imply by this statement that an adjustment in C&S's route south of Havana is required since, in addition to C&S, operations south of Havana are conducted by other American flag carriers as well as foreign air carriers. However, the high level of mail pay for C&S indicates that it may be appropriate to examine the route structure under which international service south of Havana is being provided by the United States carriers in general, for the purpose of determining whether a realignment of routes in that area might result in reducing the dependency upon the United States Government for mail pay support without a corresponding reduction in the quality of such services. Accordingly, while we do not intimate any definite view as to whether such a realignment may or may not be proper, we have instructed the staff to include the Caribbean area for scrutiny along with the present studies of the domestic route structures. If, upon completion of such studies action with regard to such structure appears warranted, we shall then take such action by formal order and proceeding.

145 C & S has requested a mail rate formula which will provide mail compensation in accordance with our determination on the basis of estimated available seat-miles flown. In view of the carrier's request, we will establish for the period on and after December 16, 1950 a rate which

is calculated to produce the annual amount of mail pay prescribed herein, will be reasonable in terms of the schedule pattern recognized in this opinion, and will change in relation to fluctuations in the volume of service which may be offered.

In order to insure that C & S will receive the amount of mail pay intended by our order, to provide an effective safeguard against overpayment by reason of schedules operated in excess of those found to be required, and finally to distribute mail pay evenly from month to month throughout the year, the recognized available seat-miles over a four-week or twenty-eight day period will be used as a base monthly standard available seat mileage. Accordingly, a base rate of 3.41 cents per standard available seat-mile with a maximum monthly capacity of 4,529,000 standard available seat-miles is found to be the fair and reasonable mail rate for the period on and after December 16, 1950.

CONCLUSION

On the basis of the foregoing considerations, we find that the fair and reasonable rates of compensation to be paid to C & S for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith between the points on its Latin American routes between which the carrier is presently or hereafter may be authorized to transport mail by its certificates of convenience and necessity are as follows:

- 146 A. For the period November 1, 1946—December 15, 1950, inclusive, the sum of \$3,645,000.¹⁵

¹⁵ This amount is equivalent to a rate of 78.51 cents per recognized revenue plane mile flown in scheduled service over the international system. For administrative purposes, the breakdown of mail compensation by periods is as follows:

November 1, 1946—December 31, 1946	152,000
January 1, 1947—June 30, 1947	291,584
July 1, 1947—December 31, 1947	296,416
January 1, 1948—June 30, 1948	358,032
July 1, 1948—December 31, 1948	361,968
January 1, 1949—June 30, 1949	539,032
July 1, 1949—December 31, 1949	547,968
January 1, 1950—June 30, 1950	544,488
July 1, 1950—December 15, 1950	553,512
Total	3,645,000

B. For the period on and after December 16, 1950:

For each calendar month an effective rate per designated mile flown obtained by dividing by the designated miles flown during the month the product of 3.41 cents times the lower of 4,529,000 or the standard available seat-miles flown in scheduled passenger service during the month. For the period from December 16, 1950 to December 31, 1950, the mail rate shall be derived by dividing by the designated miles flown therein the product of 3.41 cents times the lower of 2,264,500 or the standard available seat-miles flown in scheduled passenger service during the period.

The available seat miles flown in scheduled passenger service during the month shall be computed by multiplying the scheduled mileage flown in passenger service during the month with each aircraft type by the standard available seats for that type as specified below:

Aircraft Type	Seats
DC-3	21
DC-4	44
Constellation	52

The aforesaid rates per airplane mile shall be applied to, and the designated mileage flown shall be computed on, the direct airport-to-airport mileage between points served for the carriage of mail on each trip flown on a schedule designated or ordered to be established by the Postmaster General for the carriage of mail, and the scheduled mileage flown shall be computed on the direct airport-to-airport mileage between points actually served on each trip flown in scheduled passenger service, including all trips operated as extra sections thereto.

The compensation provided above should be inclusive of, and not in addition to, the mail compensation received by the carrier for the transportation of mail on and after November 1, 1946 over its Latin American routes.

An appropriate order will be entered.

CHICAGO AND SOUTHERN AIR LINES, INC.—INTERNATIONAL OPERATIONS

Traffic Statistics as Reported and as Adjusted
For the Period November 1, 1946–December 15, 1950¹

	As Reported		As Adjusted	
	11-1-46 to 6-30-49	7-1-49 to 12-15-50	11-1-46 to 12-15-50	7-1-49 to 12-15-50
<i>Capacity Operated (000)</i>				
Revenue plane miles	2,072	2,912	4,984	2,571
Available seat-miles—reported	96,416	119,917	216,333	—
—standard ²	90,778	125,356	216,134	110,789
Available ton-miles—reported	10,586	14,958	25,544	—
—standard ³	12,385	17,038	29,423	15,062
<i>Capacity Utilized (000)</i>				
Revenue passenger-miles	33,860	40,113	73,973	38,471
Revenue ton-miles:				
Passenger (@ 215 lbs.)	3,641	4,312	7,953	4,136
Freight	374	804	1,178	774
Excess baggage	102	146	248	141
Foreign mail	2	8	10	8
U. S. mail	12	42	54	42
Total	4,131	5,312	9,443	5,101
<i>Load Factors (Percent)</i>				
Passenger—reported	35.12	33.45	34.19	—
—standard	37.30	32.00	34.23	34.72
Over-all—reported	39.02	35.51	36.97	—
—standard	33.35	31.18	32.07	33.87
Average daily route miles in operation	1,247	2,321	1,627	2,321
Revenue ton miles per route mile per day	3.40	4.29	3.85	4.12
Average daily round trip frequency	.85	1.18	1.02	1.04
Average daily revenue hours per aircraft	6.8	8.9	7.9	7.8
Performance factor (percent)	96.91	99.51	98.40	99.55
<i>Revenue per Unit of Service (Cents)</i>				
Passenger revenue per rev. pas.-mile	7.55	7.17	7.35	7.17
Revenue per ton-mile:				
Passenger	70.23	66.74	68.34	66.67
Freight	35.96	27.91	30.47	27.91
Excess baggage	61.51	71.88	67.62	71.88
Foreign mail	200.00	200.00	200.00	200.00

¹ Scheduled and nonscheduled operations.

² Standard capacities: DC-3, 21 seats; DC-4, 44 seats.

³ Standard available tons: DC-3, 2.4 tons; DC-4, 6 tons.

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONS

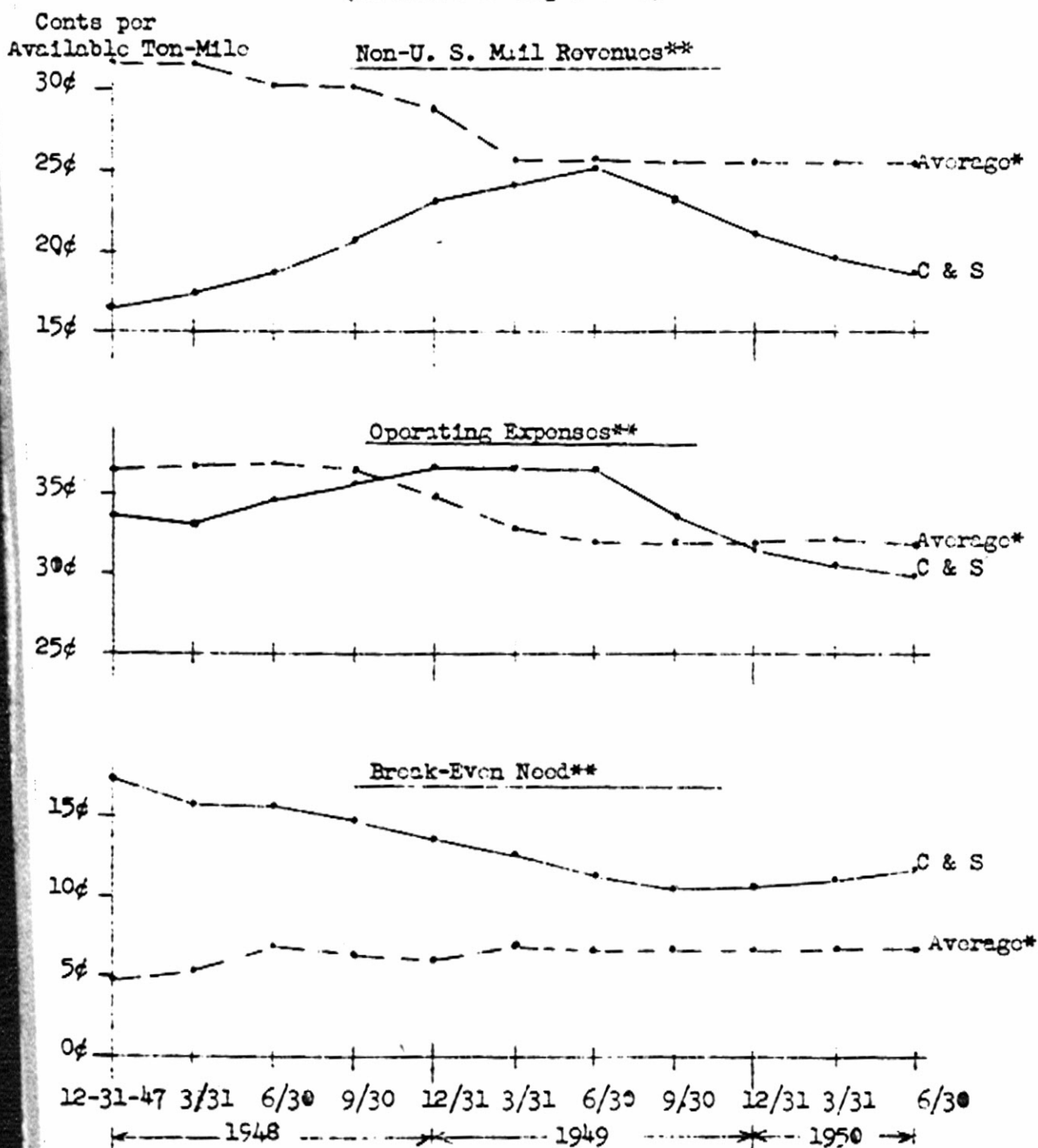
Comparisons of Traffic Density with Other Carriers

U. S. Flag International Carrier	Revenue Ton-Mile per Route Mile per Day Year Ended	
	Sept. 30, 1949	Sept. 30, 1950
Pan American—LAD	17.4	17.8
AAL—Mexico	14.5	15.2
NAL—Havana	11.4	14.8
Panagra	5.7	6.1
EAL—San Juan	5.7	5.9
Chicago and Southern	4.1	4.1
Colonial	3.3	4.7
Braniff	1.7	2.0

CHICAGO AND SOUTHERN AIR LINES, INC. - INTERNATIONAL OPERATIONS

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Comparison of Revenues, Expenses and Break-Even Need
with that of Other U. S. Flag Carriers
per Standard Available Ton-Mile
(12-month moving totals)



* Arithmetic average of international operations of American, Braniff, Colonial, Eastern, National, Panagra and Pan American's Latin American Division.

** Per standard available ton-mile.

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CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONS

Financial Results as Claimed and As Adjusted for the Period
November 1, 1946—December 15, 1950
(in thousands)

	Claimed by the Carrier ¹	Adjust- ments	As Adjusted Amount	Cents per Rev. Mile
Revenue plane miles	4,984	-341	4,643	—
<i>Non-U. S. Mail Revenues</i>				
Passenger	\$5,435	\$-120 D	\$5,315	114.48
Excess baggage	168	-4 D	164	3.53
Express	—	—	—	—
Freight	359	-9 D	350	7.54
Foreign mail	20	—	20	.43
Other non-U. S. mail	30	—	30	.65
Total Non-U. S. Mail Revenues	\$6,012	\$-133	\$5,879	126.63
<i>Operating Expenses</i>				
Flying operations	\$2,285	\$-155 D	\$2,130	45.88
Direct maintenance—flight equipment	962	12 A D	974	20.98
Depreciation—flight equipment	1,250	-562 B D	688	14.82
Total Aircraft Operating Expenses	\$4,497	\$-705	\$3,792	81.68
Ground operations	\$1,646	\$ -8 D	\$1,638	35.30
Ground and indirect maintenance	636	9 C D	645	13.88
Passenger service	614	-15 D	599	12.90
Traffic and sales	1,081	-43 C D	1,350	29.08
Advertising and publicity	312			
General and administrative	768	7 C D	775	16.69
Depreciation—ground equipment	79	—	79	1.71
Total Ground and Indirect Expenses	\$5,136	\$ -50	\$5,086	109.56
Total Operating Expenses	\$9,633	\$-755	\$8,878	191.24
Profit on sale of DC-4 aircraft ²	\$ —	\$ -19 G	\$ -19	-0.41
Amortization of DC-4 integration costs	114	-3 E	111	2.40
Amortization of preoperating expenses	49	—	49	1.06
Nonoperating income and expenses ²	47	-65 F	-18	-0.39
<i>Break-Even Need</i>	\$3,831	\$-709	\$3,122	67.27

¹ Non-U. S. mail revenues and operating expenses as reported on Form 41 except for data for period 7-1-50 to 12-15-50 which were submitted by the carrier as special information. Other data as claimed by carrier.

² Minus sign indicates income.

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*Explanatory Notes**A. Direct Maintenance*

- | | |
|---|-----------|
| 1. To eliminate aircraft overhaul expenses | \$-65,908 |
| 2. Allowance for amortization of "built-in" aircraft overhaul | 101,799 |
| 3. Allowance for amortization of "built-in" engine overhaul | 30,129 |

Total	\$ 66,020
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B. Depreciation—Flight Equipment

- | | | |
|---|-----------|------------|
| 1. Elimination of value of "built-in" overhaul from DC-4 aircraft and engines: | | |
| Aircraft | \$-85,195 | |
| Engines | -30,459 | \$-115,654 |
| 2. Adjustment of reported DC-4 flight equipment depreciation expense to reflect changes in service life to 5 years, 10 percent residual value | | -424,530 |

Total	\$-540,184
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C. Revision in Allocation Bases

To reduce reported domestic operating expenses and increase reported international expenses for the period November 1, 1946 to December 31, 1947. (Order No. E-1740 of 7-1-48) The categories of cost allocations which have been revised are:

- | | | |
|------------------------------------|-----------|----------|
| 1. Ground and indirect maintenance | \$ 18,666 | |
| 2. Advertising and publicity | -18,666 | |
| 3. General and administrative | 32,666 | \$32,666 |

D. Elimination of Estimated Revenue and Expenses Applicable to the Excess Capacity

- | | |
|--|-----------|
| 1. Passenger revenue allocated on the basis of passenger-miles and average yield per passenger-mile for the year ended June 30, 1950 | \$120,523 |
| 2. Freight and excess baggage allocated on the basis of relationship to passenger revenue for the year ended June 30, 1950 | 12,800 |

Total revenue adjustments	\$133,323
---------------------------	-----------

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- | | |
|--|------------|
| 3. Flying operations expense estimated on basis of cost per revenue plane mile for the year ended June 30, 1950 | \$-155,325 |
| 4. Direct maintenance expense estimated on basis of cost per revenue plane mile for the year ended June 30, 1950 | -54,062 |
| 5. Depreciation expense as adjusted for extension of service life. This adjustment reflects only the change in DC-4 depreciation allocated to international operations | -21,508 |
| 6. Ground operations expenses estimated on basis of arrival and departures | -7,879 |
| 7. Ground and indirect maintenance. This adjustment reflects the change in the allocation between domestic and international operations | -10,149 |
| 8. Passenger service estimated on the basis of cost per passenger mile for the year ended June 30, 1950 | -14,939 |
| 9. Traffic, sales, advertising and publicity. Reasonable estimate based on the level of the other adjustments | -24,000 |
| 10. General and administrative expenses. Estimated at 8.92 percent of total adjustments excluding G & A | -25,677 |

Total expense adjustments	\$-313,539
---------------------------	------------

11. Net adjustment to break-even need		\$-180,216
		<u><u> </u></u>
E. <i>Integration Costs</i>		
International proportion of amortization of DC-4		
integration costs:		
Claimed by carrier	\$114,655	
Allowed herein	111,332	
	<u> </u>	
Adjustment		\$ -3,323
		<u><u> </u></u>
F. <i>Nonoperating Income and Expenses</i>		
To eliminate provision for foreign operations contingencies		\$-65,000
		<u><u> </u></u>
G. <i>Profit on Sale of DC-4 Aircraft</i>		
Profit on sale of DC-4 aircraft allocated to international operations		\$-19,000
		<u><u> </u></u>

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONS

Average Investment as Claimed and as Adjusted for the Period
November 1, 1946—December 15, 1950
(in thousands)

	As Claimed by C. & S.	Adjust- ments	As Adjusted
<i>Working Capital</i>			
Current assets	\$829	\$-22 A	\$807
Prepayments	—	16 A	16
Deferred charges	—	2 A	2
Total	\$829	\$- 4	\$825
Current liabilities	\$321	—	\$321
Deferred credits	—	\$ 25 A	25
Operating reserves	—	6 A	6
Total	\$321	\$ 31	\$352
Net working capital	\$508	\$-35 A	\$473
<i>Operating Property and Equipment</i>			
Flight equipment—net	479	201 B	680
Ground property and equipment—net	70	—	70
<i>Other Assets</i>			
Investments and special funds	172	-154 C	18
Prepaid and deferred items	41	-18 D	23
Capitalized preoperating expenses	—	25 E	25
Capitalized DC-4 integration expenses	—	71 F	71
Total Investment	\$1,270	\$ 90	\$1,360

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Explanatory Notes

- A. (1) To include in the computation of average work-capital all prepaid and deferred items of a current nature
- | | | |
|---------------------------------|-----------|-----------|
| Prepayment and deferred charges | \$ 17,845 | |
| Deferred credits | -25,118 | |
| Operating reserves | -6,453 | \$-13,726 |
- (2) To eliminate 21.71 percent of average international excess mail pay
- | | |
|--|---------|
| | -21,617 |
|--|---------|
- Total \$-35,343
- B. (1) To adjust the reserve for depreciation of DC-4 flight equipment to reflect change in service life \$182,687
- (2) To decrease reserve for depreciation of DC-4 aircraft and engines to conform to built-in overhaul adjustments of reported depreciation expense
- | | | |
|----------|----------|--------|
| Aircraft | \$37,937 | |
| Engines | 13,210 | 51,147 |

(3) To adjust for the unamortized balance of capitalized aircraft and engine overhaul expense to conform to overhaul expense adjustments of reported direct maintenance expense	<u>-33,010</u>
Total	<u>\$200,824</u>
C. To exclude equipment purchase funds allocated to international operations	<u>\$-153,750</u>
D. To exclude working capital items (prepayments and deferred charges) from long-term operating property prepayments	<u>\$-17,845</u>
E. Average unamortized balance of capitalized preoperating expenses	<u>\$ 24,589</u>
F. Average unamortized balance of capitalized DC-4 integration expenses	<u>\$ 71,229</u>

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONSTraffic Statistics as Estimated by the Carrier and as
Adjusted by the Staff for a Future Year

<i>Capacity (000)</i>	Carrier's Estimate	As Adjusted Amount	Basis
Revenue plane miles:			
DC-3	219	219	
L-649	1,460	1,047	
	<u>1,679</u>	<u>1,266</u>	A
Available seat-miles—carrier basis	77,593 ¹	0	
Available seat-miles—standard	80,519	59,043	B
Available ton-miles—standard	12,204	8,902	C
<i>Capacity Utilization (000)</i>			
Revenue passenger-miles	31,100	25,900	D
Revenue ton-miles:			
Passenger (@ 215 lbs.)	3,343	2,785	E
Freight	720	533	F
Excess baggage	111 ²	90	G
Foreign mail	4 ²	3	G
U. S. mail	31 ³	23	H
Total	<u>4,209</u>	<u>3,434</u>	
<i>Load Factors (percent)</i>			
Passenger—carrier basis	40.08		
Passenger—standard basis	36.28	43.87	
Over-all—standard basis	34.49	38.58	
<i>Revenue per Unit of Service (cents)</i>			
Passenger revenue per revenue pass.-mile	6.77	6.64	
Revenue per ton-mile:			
Passenger	62.97	61.76	
Freight	28.50	28.50	
Excess baggage	66.37	66.37	
Foreign mail	226.00	226.00	

¹ Based upon DC-3, 21 seats and L-649, 50 seats.² Carrier's estimated revenue divided by the yield per ton-mile experienced during the third quarter 1950.³ Experience during third quarter 1950 projected to annual basis.

- A. Based upon seven round trips per week Houston-New Orleans with DC-3; seven weekly round trips New Orleans-Havana and four weekly round trips Havana-Kingston-Caracas with L-649.
- B. Based upon 21 seats per DC-3 aircraft and 52 seats per L-649 aircraft.
- C. Standard capacities DC-3, 2.4 tons; L-649, 8 tons.
- D. Revenue passenger-miles estimated by the carrier have been adjusted by reducing the estimated traffic to and from Caracas and Kingston by 2/7 (28.6%) to reflect the 3/7 reduction (from 7 to 4 weekly flights) in scheduled service to be recognized to these two points.
- E. Estimated revenue passenger-miles multiplied by 215 lbs. converted to ton-miles.
- F. Estimated express revenue divided by the yield per ton-mile estimated by the carrier.
- G. Estimated revenue divided by the yield per ton-mile experienced July-September 1950.
- H. Average load experienced during the third quarter 1950 applied to estimated miles.

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONSFinancial Results for a Future Year
As Estimated by the Carrier and as Adjusted
(in thousands)

	Adjusted Estimate			
	Carrier's Estimate	Adjust- ments	Amount	Cents per Rev. Mile
Revenue Plane Miles	1,679	-413	1,266	—
<i>Non-U. S. Mail Revenues</i>				
Passenger	\$2,105	\$-385	\$1,720 A	135.90
Excess baggage	74	-14	60 B	4.74
Express	—	—	—	—
Freight	205	-53	152 C	12.01
Foreign mail	8	-1	7 D	0.55
Other non-U. S. mail	19	—	19 E	1.50
Total Non-U. S. Mail Revenues	\$2,411	\$-453	\$1,958	154.70
<i>Operating Expenses</i>				
Flying operations	\$1,070	\$-285	\$ 785 F	62.02
Direct maint.—flight equip.	532	-144	388 G	30.66
Depreciation—flight equip.	446	-146	300 H	23.70
Total Aircraft Operating Exp.	\$2,048	\$-575	\$1,473	116.38
Ground operations	\$ 626	\$ —	\$ 626 E	49.46
Ground and indirect maintenance	268	—	268 E	21.17
Passenger service	288	-48	240 I	18.96
Traffic and sales	472	-192	392 J	30.97
Advertising and publicity	112	—	—	—
General and administrative	296	-26	270 K	21.33
Depreciation—ground equipment	25	—	25 E	1.98
Total Ground and Indirect Exp.	\$2,087	\$-266	\$1,821	143.87
Total Operating Expenses	\$4,135	\$-841	\$3,294	260.25
<i>Break-Even Need</i>	\$1,724	\$-388	\$1,336	105.55

Explanatory Notes

- A. Estimated revenue passenger-miles times 6.64 cents, estimated average yield per passenger-mile.
- B. Relationship of excess baggage revenue to passenger revenue estimated by carrier.
- C. Estimated revenue ton-miles times 28.50 cents, estimated average yield per freight ton-mile.
- D. Reasonable estimate based on level of other revenue items.
- E. As estimated by Chicago and Southern.
- F. Cost per revenue plane mile estimated by the carrier.
- G. 1. DC-3 based on cost per revenue plane mile estimated by Chicago and Southern.
2. L-649 cost per revenue plane mile estimated at 35.00 cents per mile.
- H. Annual depreciation of two L-649 aircraft.
- I. Cost per passenger-mile estimated by Chicago and Southern.
- J. Estimated at 20 percent of non-U. S. mail revenues.
- K. Estimated at 10 percent of other cash expenses.

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Appendix No. 8

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONSFuture Period Investment
(in thousands)

	As Claimed by C & S	Adjust- ments	As Adjusted
<i>Net Working Capital</i>	\$ 916	\$-641 A	\$ 275
<i>Operating Property and Equipment</i>			
Flight equipment—net	1,887	456 B	2,343
Ground property and equipment—net	74	—	74
<i>Other Assets</i>			
Investments and special funds	34	—	34
Prepaid and deferred items	26	-26 C	—
Long-term operating property prepayments	107	-83 D	24
Total Investment	<u>\$3,044</u>	<u>\$-294</u>	<u>\$2,750</u>
	=====	=====	=====
<i>Explanatory Notes</i>			
A. (1) To reverse carrier's claimed working capital estimate			\$-916,000
(2) To provide for net working capital based upon 26.30 percent of preliminary balance sheet data as of December 31, 1950:			
Current assets		\$928,407	
Prepayments		26,752	
Deferred charges		4,330	
Total		<u>\$959,489</u>	
Current liabilities		\$584,140	
Operating reserves		11,835	
Total		<u>\$595,975</u>	
Net working capital			363,514
(3) To reduce working capital by 26.30 percent of excess mail pay			-192,779
(4) To increase working capital to include receipts from sale of two DC-4 aircraft during the first quarter of 1951 (26.30% of \$397,000)			104,411
Total			<u>\$-640,854</u>
			=====
B. (1) To add first year accrued depreciation to restore book value of aircraft to the level at the beginning of L-649 opera- tions			\$446,667
(2) To provide for the capitalization of interest on equipment purchase funds at the rate of five percent per annum for a period of six months, with one-third of the total allo- cated to international operations			9,375
Total			<u>\$456,042</u>
			=====
C. To exclude working capital items from "Other Assets"			\$-26,321
			=====
D. To eliminate unsupported long-term operating property prepay- ments			\$-83,031
			=====

Orders
Serial Number E-5385

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
Washington, D. C.

Adopted by the Civil Aeronautics Board at its office in
Washington, D. C. on the 18th day of May, 1951.

Docket No. 2564

In the matter of the compensation for the transportation
of mail by aircraft, the facilities used and useful there-
for, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.

over its Latin American Route.

Order to Show Cause

The Board having considered all of the information and data set forth, or specifically referred to, in the Statement of Tentative Findings and Conclusions, together with the Appendixes attached thereto, dated May 18, 1951, (hereinafter referred to as the "Statement"), which Statement is attached hereto and made a part hereof, and having on the basis thereof made the tentative findings and conclusions set forth in the Statement;

IT IS ORDERED, That Chicago and Southern Air Lines, Inc. is directed to show cause why the Board should not make final the findings and conclusions set forth in the Statement, and upon the basis thereof fix, determine and publish the rates set forth in said Statement as the fair and reasonable rates of compensation to be paid the carrier for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith over its Latin American routes on and after November 1, 1946:

IT IS FURTHER ORDERED, That all further procedure herein shall be in accordance with Section 302.13 of the Procedural Regulations and that any notice, as provided for in para-

graph (c)(1) of said Section 302.13, that there exists any objection to the rates set forth in the Statement or to the admissibility in evidence of any exhibits accompanying, or to the information specifically referred to in, the Statement shall be be filed with the Civil Aeronautics Board within ten days after the date of service of this Order, and if notice is filed as aforesaid, written answer and any supporting documents, as provided for in paragraphs (c)(1) and (c)(2) of said Section 302.13, shall be filed with the Board within thirty days after the date of service of this Order;

IT IS FURTHER ORDERED, That if answer is filed
 163 hereto all elements entering into the determination of fair and reasonable rates, except insofar as limited in prehearing conference, shall be in issue, and in such event the final rates shall be determined upon the record made with respect to such issues;

IT IS FURTHER ORDERED, That this order and the attached Statement of Tentative Findings and Conclusions be served upon Chicago and Southern Air Lines, Inc.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN

M. C. Mulligan
Secretary

(SEAL)

* * * * *

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2564

CHICAGO AND SOUTHERN AIR LINES, INC.
LATIN AMERICAN OPERATIONS

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith.

Decided: October 18, 1951

For policy reasons the Board will not offset the excess earnings realized from Chicago and Southern's domestic operations under a final mail rate against the carrier's "need" for mail pay resulting from operations over its Latin American route.

Provision for Federal income taxes should be based on the actual Federal income tax rate rather than the 38 percent tax rate in force prior to the current national defense emergency.

APPEARANCES:

R. S. Maurer, L. E. Black, and W. C. Stone for Chicago and Southern Air Lines, Inc.

Roy C. Frank and Eugene J. Brahm for the Post Office Department.

Arnold D. Berkeley and Allen C. Lande, Bureau Counsel.

Opinion

BY THE BOARD:

This proceeding involves the determination of final mail rates for the Latin American operations of Chicago and Southern Air Lines, Inc., hereinafter called C&S. In re-

sponse to the petition of the carrier filed on October 11, 1946, we issued a Statement of Tentative Findings and Conclusions on May 18, 1951 (Order Serial No. E-5385), proposing final mail rates for the international operations of C&S for the past period November 1, 1946-December 15, 1950, inclusive, and for the future period beginning December 16, 1950.

C&S has accepted the proposed rates, but the Postmaster General has filed objections and an Answer to the Statement of Tentative Findings and Conclusions. In accordance with the Procedural Regulations the issues raised by the objections have been defined and hearing has been held. The parties have submitted briefs to the Board, and have agreed to waive further procedural steps prior to final decision.

The parties have stipulated that no facts are in controversy and have submitted only two issues involving questions of policy and law for our decision. As expressly limited by agreement of the parties, the two issues are as follows:

1. Whether in fixing mail rates for past and future rate periods involving operations of C&S over its Latin American route, the Board should offset the excess earnings realized by the carrier's domestic routes while operating under a final mail rate.

2. Whether the Board should recognize and apply the actual Federal income tax rate, rather than a 38 percent tax rate, for the purpose of computing the tax allowance in the rates to be established for the Latin American division of C&S.

Since, except as stated above, our findings and conclusions in the Tentative Statement have not been contested as to matters entering into the determination of mail rates for this carrier, resolution of these issues is all that remains necessary for the determination of the fair and reasonable final mail rates.

248 *The Offset of Earnings of the Domestic Routes
Against The "Need" of the Latin American Routes*

During part of the past period involved in this proceeding, namely, 1948-1950, the domestic routes of C&S were operated under final mail rates which yielded the carrier an average rate of return on investment estimated at 12.5 percent. When fixing these mail rates, the Board had estimated a rate of return of 7.4 percent for the carrier from its domestic operations. In undertaking the issuance of a Statement of Tentative Findings and Conclusions for mail rates for C&S' international routes in this case we gave careful consideration to the possible offset of such excess earnings against the "need" resulting from the carrier's international operations. We decided, however, for reasons of economic policy, that no offset should be made.¹ The Postmaster General has objected to this finding, arguing that the "all other revenue" language of section 406(b) of the Act requires that the Board offset the excess earnings from domestic operations under the final rate against the "need" resulting from international operations in establishing rates applicable to both the past and future operations of the international routes. The carrier and the Bureau Counsel maintain that there is no duty of offset, and urge that none be made. In fact, Bureau Counsel questions the Board's power to offset earnings of one segment of an air carrier's operations under an unchallenged final mail rate against the "need" incurred on a different part.

249 After careful consideration of the various contentions of the parties, we conclude that we are not required to make the offset urged by the Postmaster General. Subsequent to the issuance of our Tentative Statement in this proceeding we had occasion in the *Western Air Lines, Inc.-Inland Air Lines, Inc., Mail Rates Case*,² to express an

¹ At the same time we pointed out that we had the power to institute proceedings to reduce rates and that we were having the staff make studies of C&S' earnings to determine whether such proceedings should be instituted. As a result of these studies, we issued an order on October 1, 1951 (Order Serial No. E-5747), reopening the current final mail rates for the domestic operations of C&S and six other domestic trunkline operators.

² Order Serial No. E-5467, adopted June 26, 1951.

opinion on the obligation imposed on us by the Act to consider "other revenue" for the purpose of reducing need in final mail rate proceedings. We there concluded that while we are required to take into consideration the need of a carrier for mail compensation together with "all other revenue", we believe that we are not required by section 406(b) to reduce the carrier's mail pay with any part of such other revenue if there are sound reasons for not doing so as a matter of economic policy. Reappraising that opinion in the light of this case, we consider that the same principle is applicable here in view of the policy considerations which we discuss below.

If an offset policy were adopted, the almost invariable result would be that, as in the instant case, the profits from a carrier's domestic operation would be used to sustain any international operations it might have. Recognizing this likelihood, we hesitate to burden the more robust segment of the industry with the obligations of the economically weaker part. For if the domestic air transport system can be kept financially sound, the public must ultimately benefit, putting aside any consideration of the obvious advantage of reduced rates of mail compensation. Thus, we anticipate that if the carriers' earning position continues strong, reductions in the domestic fare level will be possible, thereby giving impetus to the further development of the
 250 industry. In addition, with improved earnings, the domestic operators should be able to benefit the public and themselves with more modern aircraft, and with improved methods affording safer and more efficient operations. We cannot escape the thought that if we allow international operations to be carried on the back of domestic operations, we shall be subjecting the latter to an unjustifiable strain. Many of the domestic operators are well along the road to self-sufficiency. It is our duty to speed them on their way, not thwart them.

It also appears desirable to maintain the comparative status between those domestic operators which have foreign routes as against those which do not have foreign routes.

Since carriers fall into fairly well-defined classes, the Board is enabled to fix uniform domestic mail rates for groups of carriers provided, of course, that their comparative status is preserved by excluding consideration of any international operations. A carrier operating under a class rate has every incentive to operate efficiently because it may retain any profits it earns in excess of the estimated return to be afforded by the uniform rate. It is also administratively desirable to preserve a comparative status between carriers because the Board has been able to analyze the operations of each carrier within a class in the light of the results achieved by others within the same class. The comparison technique of rate-making has proved to be the most satisfactory and practicable available to the Board. If we were required to fix rates for both domestic and international operations at the same time, it would be difficult, if not impossible, to find a suitable basis for a comparison technique of analysis.

251 In view of the foregoing, we find that the earnings from C&S' domestic routes should not be used to offset the "need" resulting from the carrier's international routes. This conclusion stems from considerations of economic policy; we are not deciding the question of our legal power to make such an offset.

The Allowance for Federal Income Taxes

The Postmaster General objects that it is not proper to recognize in the mail rate to be paid by the Government any actual corporate tax rate increase in excess of 38 percent because such an allowance would defeat the basic purposes of the tax increases, namely, to raise the public funds necessary to meet the national defense emergency and to safeguard against further inflationary tendencies. He adds that the carrier, like other citizens, should bear its share of the increased tax burden.

Although the parties have agreed that the tax return technique which we adopted in the *Western-Inland Mail Rates Case* should be employed in this proceeding, the

Postmaster General, who strongly favored such a technique, now wishes to depart from it to the extent that he proposes to recognize only a 38 percent tax rate instead of the higher actual rate of 42 percent during 1950 and 47 percent thereafter. Bureau Counsel and the carrier oppose this contention. Under the Postmaster General's theory a tax allowance would be derived which falls short of meeting the carrier's actual tax liability as reflected on the face of the return. In view of the nature of the tax return technique of making provision for taxes, we cannot accept the Postmaster General's argument.

It is well established that in fixing the rate to be allowed a public utility for a proper income, the Federal income tax must be provided for as an operating charge. 252 The courts have followed this principle and the Board itself has followed it in all of its mail rate decisions. During the period when Federal income tax rates on corporations were gradually raised from 19 percent in 1938 to the 38 percent level prior to 1950, the Board and other regulatory agencies recognized these increases as proper operating charges in determining what rates would constitute a fair return on investment.³

As we indicated in the *Western-Inland Mail Rates Case* the purpose of the tax allowance is to afford the carrier an opportunity to realize the full rate of return which the Board has determined it should properly be granted to meet its statutory needs. Thus, we have determined in this case that the carrier is entitled to a rate of return of 7 percent for the past period and 10 percent for the future period. The Postmaster General has not demonstrated that the rates of return prescribed for C&S and carriers of its class are excessive or unreasonable under current conditions. Yet, if the carrier is taxed at the 47 percent rate, but the allowance for taxes is based on a hypothetical 38 percent rate, as the Postmaster General suggests, C&S will have after taxes a rate of return on investment of

³ Of course, our discussion of the proper Federal income tax allowance does not cover the question of excess profits taxes since they are not in issue here.

only 5.9 percent for past periods and 8.5 percent for future periods rather than the returns which the Board has found to be reasonable.

Finally, another basic flaw in the Postmaster General's argument is that he assumes an increase in corporate taxes will automatically reduce the net income of unregulated enterprises, and, therefore, that it would be unjust to permit air carriers an exemption from this general reduction in corporate net income after taxes. However, there is nothing in the recently enacted price control or tax legislation which indicates a congressional intention to reduce the profits earned either by ordinary corporations or public utilities to a level which falls below a fair and reasonable return.

CONCLUSION

In view of the foregoing, we find that the objections of the Postmaster General to the Statement of Tentative Findings and Conclusions (Order Serial No. E-5385) issued in this proceeding should be denied. However, an adjustment must be made in the rate of mail compensation for the past period. This arises from the fact that the parties have stipulated that the allowance for Federal income taxes of \$130,000 made in the Tentative Statement should be increased to \$147,000. This change results from the application of the tax return technique of determining the proper allowance for Federal income taxes instead of the "hybrid" method which was used by the Board in the Tentative Statement but which has been abandoned since that time.⁴ Accordingly, we reaffirm and hereby adopt our findings in the Statement of Tentative Findings and Conclusions, except with respect to the allowance for Federal income taxes in the past rate period and the issue of offset discussed above.

Therefore, we now find that compensation for the transportation of mail over its international routes

⁴ Adoption of the tax return technique was first announced by the Board in *Western Air Lines, Inc.-Inland Air Lines, Inc., Mail Rates*, Order Serial No. E-5467, adopted June 26, 1951.

by C&S for the period November 1, 1946-December 15, 1950, inclusive, should be fixed at \$3,662,000.

An appropriate order will be entered.

Nyrop, Chairman, Ryan, Lee, Adams, and Gurney, Members of the Board, concurred in the above opinion.

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Orders

Serial Number E-5793

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board at its office in Washington, D. C., on the 18th day of October, 1951.

Docket No. 2564

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.

over its Latin American Route.

Order Fixing and Determining the Fair and Reasonable Final Rates of Compensation for the Transportation of Mail by Aircraft

A public hearing having been held in the above-entitled proceeding, and the Board, upon consideration of the record, having issued its opinion containing its findings, conclusions, and decision, which is attached hereto and made a part hereof;

IT IS ORDERED, That the fair and reasonable rates of compensation to be paid to Chicago and Southern Air Lines, Inc., for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith between the points on its Latin American routes between which the carrier is presently or hereafter may be authorized to transport mail by its certificates of convenience and necessity are as follows:

1. For the period November 1, 1946-December 15, 1950, inclusive, the sum of \$3,662,000.¹
2. For the period on and after December 16, 1950:

For each calendar month an effective rate per designated mile flown obtained by dividing by the designated miles flown during the month the product of 3.41 cents times the lower of 4,529,000 or the standard available seat-miles flown in scheduled passenger service during the month. For the period from December 16, 1950, to December 31, 1950, the mail rate shall be derived by dividing by the designated miles flown therein the product of 3.41 cents times the lower of 2,264,500 or the standard available seat-miles flown in scheduled passenger service during the period.

256 The available seat miles flown in scheduled passenger service during the month shall be computed by multiplying the scheduled mileage flown in passenger service during the month with each aircraft type by the standard available seats for that type as specified below:

Aircraft Type	Seats
DC-3	21
DC-4	44
Constellation	52

The aforesaid rates per airplane mile shall be applied to, and the designated mileage flown shall be computed on, the direct airport-to-airport mileage between points served for the carriage of mail on each trip flown on a schedule designated or ordered to be established by the Postmaster General for the carriage of mail, and the scheduled mileage flown shall be computed on the direct airport-to-airport mileage between points actually served on each trip flown in scheduled passenger service, including all trips operated as extra sections thereto.

The compensation provided above shall be inclusive of, and not in addition to, the mail compensation received by the carrier for the transportation of mail on and after November 1, 1946, over its Latin American route.

¹ This amount is equivalent to a rate of 78.87 cents per recognized revenue/plane mile flown in scheduled service over the international system.

IT IS FURTHER ORDERED, That the aforesaid order fixing fair and reasonable rates shall be effective as of this date, all parties to the above-entitled proceeding having already waived all procedural requirements subsequent to hearing short of a final decision of the Board fixing rates herein.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN

M. C. MULLIGAN

Secretary

(Seal)

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BEFORE THE
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2564

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.

over its Latin American Route.

Petition to Reconsider

TO THE CIVIL AERONAUTICS BOARD:

The Postmaster General, pursuant to Section 302.11 of the Board's Rules of Practice, hereby petitions the Board to reconsider the ruling for mail rate-making purposes which fails to take into account the excess earnings realized by the carrier from its domestic operations when fixing and determining the true subsidy need of the carrier, Chicago and Southern, during the same period of time involved for the Latin American operation of C. & S. The ruling is set forth in the Board's Opinion and Order E-5793, of October 18, 1951, in the above-entitled rate proceeding. The said ruling is challenged herein on the grounds that:

I

The mail rate section (406(b)) of the Civil Aeronautics Act requires the Board to apply the excess earnings of the domestic system—as “other revenue”—when determining the true need of the carrier as a whole for subsidy mail compensation.

II

The Board has failed to consider the Postmaster General's contention that C. & S. has no “need” for additional compensation for its Latin American operations to the extent that C. & S. has received excess earnings from its domestic operations which meets the need requirements of the Latin American operations for the same period of time.

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III

Excess subsidy should never be deemed to be needed in order to maintain an air transport system on a sound financial basis.

IV

The Board's reason—to enable the Board to provide a uniform class mail rate for groups of carriers—used as a foundation for the rule in question is not supported by actual facts and practices.

• • • • •

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D. C. on
the 18th day of January, 1952.

Docket No. 2564

In the matter of the compensation for the transportation
of mail by aircraft, the facilities used and useful there-
for, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.
over its Latin American Route.

Order Denying Petition for Reconsideration

The Board having issued on October 18, 1951, an opinion and order¹ fixing final mail rates for both past and future periods for the Latin American operations of Chicago and Southern Air Lines, Inc.;

The Postmaster General of the United States having filed on November 19, 1951, a petition for reconsideration of this opinion and order only insofar as the Board decided not to offset the excess earnings realized by the carrier's domestic operations against the "need" on its Latin American operations, and the carrier and Bureau Counsel having filed their respective answers to the petition for reconsideration in support of the Board's decision;

The Board, upon consideration of the petition of the Postmaster General, finding that it contains no matter not previously considered by the Board herein, and that the matters set forth therein do not warrant the granting of the relief requested;

¹ Order Serial No. E-5793.

IT IS ORDERED, That the petition for reconsideration of the Postmaster General be, and it hereby is, denied.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN
M. C. Mulligan
Secretary

(SEAL)

183-A

BEFORE THE
CIVIL AERONAUTICS BOARD

Docket No. 2564

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.

over its Latin American Route.

[Excerpts From] Stipulation and Waiver Respecting Answer of the Postmaster General

WHEREAS the Board has heretofore issued in the above-entitled proceeding an Order directing the parties to show cause why the Board should not adopt the proposed rates set forth in the Statement of Tentative Findings and Conclusions, accompanying the said Order Serial Number E-5385, adopted May 18, 1951, in Docket No. 2564;

AND WHEREAS the Post Office Department having filed a notice of objections to said Order, and its accompanying Statement of Tentative Findings and Conclusions, and an Answer, dated June 14, 1951 filed pursuant to Section 302.13(c) of the Procedural Regulations of the Board, which said Answer objected to the Board's method of computing Federal income taxes for the past and future rate-making periods involved, and also to the Board's refusal to take into account the excess earnings of the domestic division when considering the needs of Chicago and Southern's international division;

183-B AND WHEREAS all of the parties desire to expedite the final disposition of this rate proceeding they have decided to waive certain procedural steps and enter into a stipulation concerning the factual issues raised by the said Answer, leaving the legal and policy issues thereby presented for determination by the Board;

NOW THEREFORE this stipulation entered into this 31st day of July, 1951, between the parties in the above-entitled proceeding witnesses that Chicago and Southern Air Lines, Inc., the Post Office Department and Bureau Counsel, do agree and consent, as follows:

• • • • •

183-C (5) That the total earnings, in excess of whatever rate of return on recognized investment shall be adopted as a standard for this purpose by the Board, realized by the domestic division of Chicago and Southern Air Lines, Inc. during the past period commencing January 1, 1948, and extending through December 15, 1950 were as shown in the computations made by the staff, which are attached hereto as Appendix II, and that such computations be made a part of this Stipulation;

• • • • •

183-I

Appendix II

CHICAGO AND SOUTHERN AIR LINES, INC.

Computation of Earnings from Domestic Operations to be Offset in
the Mail Rate for the International Division
Years 1948-1950
(in thousands)

	1948	1949	1950	Total
Domestic Operating Net Profit:				
As reported	\$ 446	\$ 471	\$ 470	\$1,387
Adjustments (see page 2)	69	115	31	215
Total	<u>\$ 515</u>	<u>\$ 586</u>	<u>\$ 501</u>	<u>\$1,602</u>
Investment	\$4,150	\$4,035	\$4,617	\$4,267
Rate of Return	12.41%	14.52%	10.85%	12.51%
Earnings Above:				
8 percent	\$ 183	\$ 263	\$ 132	\$ 578
10 percent	100	182	39	321

183-J

CHICAGO AND SOUTHERN AIR LINES, INC.

Computation of Net Profit Adjustments
Years 1948-1950
(in thousands)

	1948	1949	1950	Total
<i>Expense Additions</i>				
Adjustment of DC-3 depreciation to reflect change in service life	\$125	\$ 63	\$ —	\$188
DC-4 equipment integration costs	36	26	37	99
Accounting change in allocation of joint expenses due to excess capacity disallowance in international operations:				
Depreciation	—	—	21	21
Ground Operations	—	—	8	8
Ground and indirect maintenance	—	—	10	10
General and administrative exp.	—	—	23	23
Total	<u>\$161</u>	<u>\$ 89</u>	<u>\$ 99</u>	<u>\$349</u>
<i>Expense Deductions</i>				
Adjustment of DC-4 depreciation to reflect changes in service life	\$148	\$204	\$103	\$455
Profit on sale of DC-4 aircraft allocated to domestic system	—	—	27	27
DC-3 depreciation charged by carrier ¹	82	—	—	82
Total	<u>\$230</u>	<u>\$204</u>	<u>\$130</u>	<u>\$564</u>
Total Adjustment to Reported Net Profit	<u>\$ 69</u>	<u>\$115</u>	<u>\$ 31</u>	<u>\$215</u>

¹ After domestic rate order of July 1, 1948 C&S changed service life of DC-3 aircraft from common retirement date of 6-30-47 to 12-31-48.

**In the United States Court of Appeals
for the District of Columbia Circuit**

JESSE M. DONALDSON, Postmaster General
of the United States, and

THE UNITED STATES OF AMERICA on behalf of the
Postmaster General, *Petitioners,*

v.

CIVIL AERONAUTICS BOARD, *Respondent.*

On Petition for Review of Order of the Civil Aeronautics Board

United States Court of Appeals
For the District of Columbia Circuit

BRIEF FOR PETITIONERS

FILED JUL 9 1952

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Washington 25, D. C.*

QUESTIONS PRESENTED

Chicago and Southern Air Lines ("C & S") conducts both domestic and Latin American operations. In 1948 the Civil Aeronautics Board fixed a final prospective subsidy mail rate for C & S's domestic operations which it estimated would yield the carrier a net return after taxes of 7.4% on that portion of its property allocable to domestic operations. Actual operations under that rate, however, resulted in an average return on domestic operations for the years 1948 through 1950 of 12.51%, or \$654,000 more than a 7.4% rate of return would have produced. In 1951 the Board, in fixing subsidy mail pay for those years for C & S's international operations, refused to offset the excess profit of \$654,000 attributable to domestic flights. Section 406(b) of the Civil Aeronautics Act directs the Board, in fixing mail pay, to "take into consideration, among other factors, * * * the need of each such air carrier for compensation for the transportation of mail sufficient * * * together with all other revenue of the air carrier * * *" to enable the carrier to "maintain and continue the development" of a national air transportation system. The questions presented are:

1. Whether the Board is empowered under Section 406 (b) of the Act to award a subsidy in the form of "need mail pay" which is greater than the carrier's "need."

2. Whether Section 406(b) authorizes the Board to award "need" mail pay on the basis of the needs of particular operating divisions of a carrier without regard to the need of the carrier as a whole.

3. Whether Section 406(b) requires the Board, in determining a carrier's "need" for subsidy, to offset *all* other revenue of the carrier.

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In the United States Court of Appeals for the District of Columbia Circuit

No. 11,351

JESSE M. DONALDSON, Postmaster General
of the United States, and

THE UNITED STATES OF AMERICA on behalf of the
Postmaster General, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

On Petition for Review of Order of the Civil Aeronautics Board

BRIEF FOR PETITIONERS

JURISDICTIONAL STATEMENT

The jurisdiction of this Court is invoked under Section 1006 of the Civil Aeronautics Act of 1938, 52 Stat. 1024, 49 U.S.C. 646. The final order of the Civil Aeronautics Board, fixing mail pay for Chicago and Southern Air Lines for its Latin American operations, was entered on October 18, 1951 (J. A. 58).¹ The petition to review that order was filed on March 18, 1952, within 60 days after the Board denied the Postmaster General's petition for reconsideration on January 18, 1952 (J. A. 62.)² Section 1006, *supra*;

¹ Throughout this brief, the joint appendix will be cited as "J. A."

² The Postmaster General is required to pay air carriers for transporting air mail, out of funds appropriated by Congress for that purpose, at the rates fixed by the Board. Section 406(a). He participates in all air mail pay proceedings before the Board, and serves as the protector of the public interest in such proceedings. *Seaboard & Western Air Lines v. Civil Aeronautics Board*, 86 U.S. App. D.C. 64, 67-68, 181 F. 2d 515, 518-519, certiorari denied 339 U.S. 963. The Postmaster General thus has a substantial interest in the order under review within the meaning of Section 1006 of the Act. Cf. *Far East Conference v. United States*, 342 U.S. 570, 576.

Braniff Airways v. Civil Aeronautics Board, 79 U. S. App. D. C. 341, 147 F. 2d 152. The opinions of the Civil Aeronautics Board have not been published in bound form; they are set forth in the joint appendix, pages 6-60.

STATEMENT OF THE CASE

Chicago and Southern Air Lines ("C & S") is a certificated air carrier conducting both domestic and Latin American operations.³ The petition for review challenges an order of the Civil Aeronautics Board which fixed "need" (i.e. subsidy) mail pay covering the carrier's Latin American routes. It is petitioners' contention that the Board violated the plain terms of Section 406(b) of the Civil Aeronautics Act by failing to offset C & S's "excess" profits on its domestic operations in determining the carrier's subsidy "need" on its foreign routes. The underlying facts are undisputed.

Separate proceedings were conducted by the Board to fix C & S's domestic and foreign mail rates. Final domestic rates were fixed in July, 1948. *Chicago and Southern Airlines, Mail Rates*, 9 C.A.B. 786. They included a past rate for the period January 1, 1946, through December 31, 1947 (not involved in this case), and a prospective rate for the period commencing January 1, 1948.⁴ The Board estimated that the future rate would yield C & S a net return after taxes of 7.4% on that part of its investment allocable to domestic operations. Actual operations under the rate, however, resulted in an average return on domestic operations for the years 1948 through 1950 of 12.51%.⁵ This was \$654,000 more than a 7.4% rate of return would have produced.

³ C & S's domestic routes are between Chicago/Detroit/Kansas City and Houston/New Orleans. See 9 C.A.B. 786, 789-90. The carrier's international routes are between Houston/New Orleans and various points in the Caribbean and Caracas, Venezuela (J. A. 7).

⁴ Both the domestic and the international rates were fixed upon the basis of an allocation of the carrier's expenses and investments common to both domestic and foreign services. 9 C.A.B. at 803-804, 809, 812-813; J.A. 17-18, 21, 28-29).

⁵ J. A. 53. Figures relating to C & S's domestic rate of return during those years are contained in a stipulation entered into during the Board proceedings in the instant case (J. A. 63).

On October 18, 1951, the Board issued its opinion and order fixing final subsidy mail pay rates for C & S's Latin American operations (J.A. 51).⁶ Rates were fixed retroactively for the period from November 1, 1946, to December 15, 1950, and prospectively from December 16, 1950 (J.A. 59).⁷ The rates were fixed to give the carrier a rate of return after taxes on its property allocable to foreign operations of 7% for the past period (J. A. 23), and 10% for the future (J. A. 30).

In fixing the rates, both retroactively and prospectively, the Board refused to offset C & S's "excess" profits on its domestic routes against the carrier's "need" resulting from its international operations (J. A. 53-55).^{7a} The Board reaffirmed and applied the principle it had previously enunciated in the contemporaneous *Western Airlines* case⁸—that Section 406(b) of the Civil Aeronautics

⁶ C & S was certificated on its Latin American routes on May 17, 1946. *Latin American Air Service*, 6 C.A.B. 857, 927 (1946). Service over these routes was inaugurated November 1, 1946 (J.A. 8). A petition to fix mail rates for these routes was filed by C & S in October, 1946 (*ibid.*) On May 18, 1951, the Board issued a statement of tentative findings and conclusions proposing final rates for C & S's foreign operations (J. A. 6).

The tentative findings concluded that the carrier's "excess" domestic earnings should not be offset "against the need which would otherwise be found to exist in relation to C & S's international operations" because "policy considerations" rendered such an offset "inappropriate" (J. A. 19). The Board stated that the airline industry could best achieve economic self-sufficiency, from the mail rate standpoint, by placing carriers on final future rates as soon as possible; that determination of a final future rate is an "exacting" task where the carrier operates only in the domestic or in the foreign field; and that unless final future domestic rates could be fixed without simultaneously determining international rates, "it may often prove to be impossible to fix any permanent rate for the carrier for an extended period of time" (J. A. 20).

The Postmaster General filed objections to the proposed rates on the ground, *inter alia*, that the Board improperly refused to offset the "excess" domestic earnings (J. A. 52).

⁷ Temporary foreign mail pay rates had been fixed by the Board in March, 1947 (7 C.A.B. 985), and May, 1948 (9 C.A.B. 924).

^{7a} The Board's refusal to offset the excess profits for the past period resulted in the carrier receiving an additional \$654,000 in subsidy mail pay (cf. J. A. 65).

The amount of such excess for future periods has not been calculated. However, petitioners' challenge of the future rates relates only to the period December 16, 1950, to September 30, 1951. Effective October 1, 1951, C & S's domestic rates were substantially reduced. *Chicago and Southern Air Lines, Domestic Operations, Mail Rates*, Docket No. 5144, Order No. E-5956, December 19, 1951. The Board order instituting those proceedings recited that the then existing domestic rates appeared "to have become or will be excessive." *Ibid.*, Order E-5747, Oct. 1, 1951.

⁸ *Inland Air Lines-Western Air Lines, Mail Rates*, Docket No. 2870, et al., Order No. E-5467, June 26, 1951, petition to review pending *sub nom. Donaldson v. Civil Aeronautics Board*, C.A.D.C., No 11,259.

Act does not require it to reduce the carrier's mail pay by offsetting any part of the carrier's other revenue "if there are sound reasons for not doing so as a matter of economic policy" (J. A. 54). The Board stated that if profits from domestic operations were used to "sustain" international flights, the "more robust" domestic segment of the industry would be burdened with the obligations of the "economically weaker" international segment. By maintaining the domestic segment in a "financially sound" position, the Board continued, the public will benefit through lower fares, reduced mail compensation, more modern aircraft and improved operating methods (*ibid.*). The Board further stated that it was "desirable" to maintain the "comparative status" between domestic operators with and those without foreign routes, in order to permit the Board to continue using the comparison technique for fixing class rates for domestic carriers (J. A. 54-55).⁹

A petition for reconsideration filed by the Postmaster General, again challenging the propriety of the Board's failure to offset the "excess" domestic earnings (J. A. 60-61), was denied by the Board without opinion (J. A. 62).

STATUTE INVOLVED

The Civil Aeronautics Act of 1938, 52 Stat. 977, as amended, 49 U. S. C. 401 *et seq.*, provides in pertinent part as follows:

Section 406(a) The [Board] * * * is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, * * * and the rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft. [49 U. S. C. 486(a).]

⁹ The Board stated that its decision not to make the offset stemmed from "considerations of economic policy," and that it was not deciding the question, raised by Board counsel (J. A. 53), of its power to make the offset (J. A. 55).

Section 406(b) In fixing and determining fair and reasonable rates of compensation under this section, the [Board] * * *, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the [Board] * * * shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense. [49 U. S. C. 486(b).]

STATEMENT OF POINTS

The Civil Aeronautics Board erred:

1. In failing to apply the \$654,000 "excess" profits from C & S's domestic operations for 1948 through 1950 in determining the carrier's need for subsidy mail pay on its Latin American routes during those years.
2. In fixing need mail pay for C & S's Latin American operations without regard to the need of the carrier as a whole.
3. In holding that Section 406(b) of the Civil Aeronautics Act authorizes it to exclude, because of policy considerations, any portion of a carrier's "other revenue" in determining a carrier's subsidy need.

SUMMARY OF ARGUMENT

I

Section 406(b) of the Civil Aeronautics Act, which formulates the standards to be followed by the Civil Aeronautics Board in fixing "fair and reasonable" mail pay rates, distinguishes between compensation for carrying the mail, and subsidy payments to insure the development of a national system of air transportation in accordance with the statutory objectives. The Board has recognized this distinction; it fixes mail pay on either a "service" (i.e., compensatory) or on a "need" rate. The "need" rate is an acknowledged subsidy. In fixing that rate, however, the Board cannot award subsidy in an amount in excess of what the carrier "needs," as that term is defined in Section 406(b). The Act does not authorize the Board to award a subsidy which gives the carrier an over-all rate of return greater than the aggregate of the needs of its individual divisions.

II.

The need referred to in Section 406(b) is the need of the carrier as a whole, and not the need of particular operating divisions. Prior to the instant case, the Board has consistently recognized that principle. The decision under review departs from this construction. For, by refusing to offset C & S's "excess" profits on its domestic routes, the Board has determined the carrier's need for subsidy on its international operations as if the latter were those of a separate carrier. The Board's power administratively to fix rates separately for different operating divisions of a carrier does not override the statutory limitation that the total subsidy awarded cannot exceed the need of the carrier as a whole.

III

Section 406(b) defines a carrier's need as the amount required to accomplish the statutory objectives after offsetting "all other revenue" of the carrier. The Act thus

requires that *all*—not some—other revenue be offset in determining a carrier's need, and does not authorize the Board to exclude any part of such other revenue because of policy considerations. A statute providing for subsidization of private enterprise at public expense should be strictly construed. The Board's treatment of the "all other revenue" clause in Section 406(b) could lead to the emasculation of the entire need standard.

ARGUMENT

I

Subsidies in the Form of Mail Pay May Be Granted Only to the Extent of the "Need" of the Carrier

Section 406(a) of the Act directs the Board to fix "fair and reasonable" rates of compensation for the transportation of mail by aircraft. Section 406(b) provides that in determining such rates, the Board "shall take into consideration," *inter alia*,

* * * the need of each such carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

The Act thus distinguishes between the carrier's respective needs for compensation sufficient (1) to insure the transportation of mail, and (2) to enable the carrier to aid the development of a national system of air transportation.

The Board has recognized this distinction in fixing mail pay rates. Such rates may be calculated on what the Board describes as a "service" basis or a "need" basis. "Service" payments are intended to provide the carrier with fair compensation for carrying the mail, and sup-

posedly contain no subsidy elements.¹⁰ A "need" rate, on the other hand, bears no relationship to the carrier's services in carrying the mail,¹¹ but is an acknowledged subsidy to maintain the carrier as an efficient going-concern. The "need" rate is fixed by the Board at a level to provide the carrier with sufficient income to (1) meet its entire operating charges, (2) pay its taxes, and (3) earn a fair rate of return on its total invested capital.¹² Since, however, the carrier is required to operate under "honest, economical, and efficient management," the Board disallows excessive or improper expenditures in determining the carrier's need.

"Section 406(b) of the Act * * * requires that mail pay shall be awarded in an amount corresponding to the statutory 'need' for such compensation as a means of maintaining and continuing the development of air transportation in the public interest * * *."¹³ Although need is not the only factor to be considered, it plainly is a mandatory, limiting feature, i.e., the Board cannot award mail pay in an amount in excess of what the carrier needs.

Without the "carefully worded 'need' formula which the Act sets for the Board's guidance in fixing the air mail 'compensation' "¹⁴ the Board would be left without any major standard to guide it in fulfilling its statutory duty

¹⁰ *Eastern Air Lines, Mail Rates*, 3 C.A.B. 733, 755, 760 (1942). "Service" rate payments are not limited to reimbursement of expenses of carrying the mail, but also include a fair profit to the carrier for rendering the service. *Id.* at 755-756.

¹¹ For example, the Board has allocated "need" payments to particular routes although no mail was carried on them. *Chicago and Southern Air Lines, Mail Rates*, 3 C.A.B. 161, 190 (1941).

¹² *Pioneer Air Lines, Mail Rates*, 8 C.A.B. 175, 187 (1947). The Board generally allows a 7% return for past periods on both domestic and international operations (*Western Air Lines, Mail Rates*, Docket No. 2870, Order No. E-4870, November 27, 1950, mimeographed p. 47; J.A. 23). For future periods, the return generally is 8% for domestic operations (*Chicago and Southern Air Lines, Domestic Operations, Mail Rates*, Docket No. 5144, Order No. E-5869, November 15, 1951) and 10% for foreign operations (J.A. 30).

¹³ *Western Air Lines, Mail Rates*, Docket No. 5148, Order No. E-6295, April 7, 1952, at mimeographed p. 11. Accord: *American Airlines, Mail Rates*, 3 C.A.B. 323, 335-338 (1942); *Pan American Airways, Alaska Mail Rates*, 6 C.A.B. 61, 67 (1944); *Pan American Airways, Latin-American Mail Rates*, 6 C.A.B. 85, 91 (1944); *Pan American Airways, Trans-Pacific Mail Rates*, Docket No. 2147, Order No. E-5882 (November 21, 1951, mimeographed p. 21).

¹⁴ *American Airlines, Mail Rates*, 3 C.A.B. 323, 335 (1942).

of using mail payments as a device for developing air transportation. See Section 406(b); cf. *American Airlines, Mail Rates*, 3 C.A.B. 323, 335. The statutory mandate "shall take into consideration," read in the context of language which carefully formulates the elements to be considered by the Board in determining a carrier's need, cannot be construed as a grant of unlimited discretion to the Board to accept or reject the need criterion as it sees fit. Congress could scarcely have intended that the Board, after determining a carrier's need for revenue in accordance with the statutory standards, might grant a subsidy—described by the Board itself as "need" mail pay—in excess of such need.

The Board's construction of the Act, however, would give a carrier subsidy in excess of its actual need. In the instant case the Board awarded domestic "need" subsidy which it estimated would yield a return after taxes for the years 1948-1950 of 7.4% on property allocable to domestic operations. In fixing foreign subsidy pay, it gave the carrier a 7% rate of return after taxes for those years. Thus the Board in effect found that C & S "needed" a 7.4% return on domestic and a 7% return on foreign operations.

The whole cannot exceed the sum of the parts; the carrier's total need cannot add up to more than the total of the needs of each division. Yet the result reached by the Board in this case had precisely that effect. For, by treating C & S's domestic profits as if the \$654,000 "excess" had not in fact been earned, the Board has awarded subsidy mail pay that gives the carrier an overall return during those years considerably in excess of 7.4%

Hindsight now indicates that in the period 1948-1950 C & S received a subsidy for its domestic routes substantially in excess of its actual need. The carrier cannot complain if its foreign subsidy is accordingly limited to reflect its total overall need. That need—and no more—is what Section 406(b) entitles it to. Offsetting the excess domestic profits would not deny C & S a fair rate of return on each of its divisions. On the contrary, the carrier would

still be receiving a 7.4% return on its domestic and a 7% return on its international operations—rates that the Board has found to be fair. Under such circumstances, the carrier has no claim to further subsidy.¹⁵ Surely the Act does not contemplate that a carrier is to be given a subsidy which produces an overall rate of return substantially greater than the aggregate of the needs of its individual divisions.

II

The "Need" Referred to in Section 406(b) is the Need of the Carrier as a Whole, and Not the Need of Particular Operating Divisions.

The Board's opinion does not reject the view that "need" is a limiting factor. But it states "that the earnings from C & S' domestic routes should not be used to offset the 'need' resulting from the carrier's international routes" (J. A. 55). The result is to compartmentalize the carrier for mail pay purposes in a manner not authorized by the statute.

Section 406(b) makes it abundantly clear that the "need" referred to is the need of the carrier as a whole, and not the need of particular operating divisions of the carrier. The need clause begins with a reference to the need of "each such air carrier." The "other revenue" clause similarly refers to all other revenue of "the air carrier," and speaks of compensation which, together with such other revenue is sufficient to enable "such air carrier" to carry out the statutory objectives. The Act thus establishes the air carrier—and not particular routes or divisions thereof—as the "primary unit around which the national air transportation system was to be developed through the instrumentality of air mail compensation." *Chicago and Southern Air Lines, Mail Rates*, 3 C.A.B. 161, 190.

Until its decision in the instant case the Board consistently recognized this principle. In the *Chicago and*

¹⁵ Cf. *Dayton Goose Creek Ry. Co. v. United States*, 263 U.S. 456, 481-483; *Northern Pacific Ry. Co. v. North Dakota*, 236 U.S. 585, 604.

Southern case, *supra*, the Board, in deciding that it could award subsidy mail pay covering routes on which no mail was carried, flatly held:

The need [referred to in Section 406(b)] is that of the air carrier as ^awhole and not that of any particular geographical division of its operations. [*Ibid*].

This view was reasserted in a number of subsequent cases involving mail pay for both domestic and international operations.¹⁶ In the 1944 *Pan American Mail Pay* case, the Board, specifically reaffirming its holding in the *Chicago and Southern* case, held that the carrier had no "need" for subsidy mail pay on its Alaska division because excess earnings from its more profitable divisions greatly exceeded the Alaska division's requirements. *Pan American Airways, Alaska Mail Rates*, 6 C.A.B. 61, 67. This long-standing and hitherto consistent administrative construction of the Act by the agency charged with its administration is entitled to great weight. *United States v. American Trucking Association*, 310 U.S. 534, 549; *Norwegian Nitrogen Products Co. v. United States*, 288 U.S. 294, 315; cf. *Federal Power Commission v. Panhandle Eastern Pipe Line Co.*, 337 U.S. 498, 513.¹⁷

The Board's decision in the instant case departs from this settled administrative construction of the Act. For, by refusing to offset C & S's excess earnings on its domestic routes in determining the carrier's subsidy need on its foreign operations, the Board treats the Latin American routes as wholly isolated from the carrier's other activities. In other words, the Board has viewed C & S's Latin American operation as if it were that of a separate carrier. Such a construction of the Act flies in the face of the specific directive in Section 406(b) that the Board is

¹⁶ *Delta Air Corporation, Mail Rates*, 3 C.A.B. 261, 271 (1942); *Pan American Airways, Latin-American Mail Rates*, 3 C.A.B. 657, 670 (1942); *Eastern Air Lines, Mail Rates*, 3 C.A.B. 733, 739-740 (1942); *Pennsylvania-Central Airlines, Mail Rates*, 4 C.A.B. 22, 28 (1942); cf. *American Airlines, Mail Rates*, 3 C.A.B. 323, 339 (1942); *Transcontinental & Western Air, Mail Rates*, 4 C.A.B. 139, 143 (1943).

¹⁷ In the *Panhandle* case, the Court, in holding that the Commission had no power under the Natural Gas Act to regulate dealings in gas acreage, pointed out that for more than ten years the Commission had never claimed that power.

to determine the need of the "air carrier"—not the need of a particular operating division.

As we demonstrate in point III, *infra*, Section 406(b) requires the Board, in determining a carrier's need, to offset all other revenue of the carrier. If the Board were permitted to award subsidy mail pay to meet the need of particular operating divisions without regard to the carrier's over-all needs, that requirement would be thwarted. For, if the Board could thus segmentize need, consistency would seem to require that such need should be determined by offsetting only such other revenue as was attributable to the particular division concerned.¹⁸ Section 406(b), however, refers to "*all* other revenue of *the* air carrier." If the clear and unambiguous meaning of those words is to be given its normal effect, the word "need" can only mean the need of the carrier as a whole—as the Board has heretofore consistently held.¹⁹

We are not questioning the Board's power administratively to fix rates separately for different operating divisions of a carrier. We do, however, challenge the Board's position that in determining subsidy for a particular division it can ignore the operating results of other divisions during the same period. The power to treat divisions as separate entities for rate-making purposes does not override the statutory limitation that the *total* subsidy awarded cannot exceed the need of the carrier as a whole. By administratively fixing separate rates for different divisions, the Board cannot give the carrier a greater subsidy than it would receive if rates for all divisions were fixed together.²⁰

¹⁸ The result would always redound to the carrier's benefit and the taxpayer's loss, since mail pay would be used to make up deficits on unprofitable operations, and all revenue from particularly profitable operations would go to the carrier. A carrier whose overall position was excellent could demand and receive need mail pay for one unprofitable segment of its operations.

¹⁹ *Supra*, p. 11.

²⁰ The Board's own experience demonstrates that it is administratively feasible to fix separate rates for particular divisions, and still give effect to the overall need limitation. In the *Pan American* mail rate case, *supra*, separate rates were fixed for the carrier's transatlantic, Alaska, Pacific and

III

Section 406(b) Requires the Board, in Determining the Need of the Carrier for Subsidy, to Offset All Other Revenue of the Carrier

In fixing C & S's subsidy for its international routes for the period November 1, 1946, to December 15, 1950, the Board first calculated that the carrier needed \$3,122,000 in mail pay in order to break even on its international operations (J.A. 19). It then determined the carrier's recognized investment for the period to be \$1,360,000 (J.A. 23). In making these calculations, the Board made various adjustments in the carrier's actual operating results to reflect the statutory concept of "honest, economical, and efficient management." The Board allowed the carrier a return of 7% on such recognized investment, or \$393,000 (J.A. 23). To this was added \$147,000 covering Federal income taxes (J.A. 57). The total mail pay thus computed was \$3,662,000 (J.A. 58).

The Board's refusal to offset the carrier's "excess" profits on its domestic routes (\$654,000) was made in the course of calculating the carrier's break-even point. In determining not to offset these excess revenues, the Board did not hold that C & S "needed" the additional \$654,000. Instead, it merely concluded that such excess profits—admittedly "other revenue"—"should not be used to offset the 'need' resulting from the carrier's international routes" (J.A. 55). This conclusion was grounded on the Board's view that although it is required under Section 406(b) to take all other revenue into consideration in determining the need for mail pay, it may nonetheless refrain, in its discretion, from reducing "the carrier's mail pay with any part of such other revenue if there are sound

Latin American divisions. 6 C.A.B. 59, 61, 83, 85. The Board calculated the "need" of the Alaska and Pacific divisions in terms of the amount needed over and above compensatory mail pay. However, the need of those two divisions was met by offsetting the "excess" earnings from other divisions, and the carrier was not given any need payments on these divisions. 6 C.A.B. 65-69, 78, 89.

reasons for not doing so as a matter of economic policy" (J.A. 54).²¹

We submit that this construction of Section 406(b) by the Board is unwarranted. The intent of Congress reflected in that Section is that a carrier is to receive only such mail pay as it "needs," and that such "need" is to be determined by offsetting *all* its other revenue. Section 406(b) defines the need for subsidy as an amount which is sufficient "together with all other revenue of the air carrier," to enable the carrier to meet the statutory objectives. In other words, the Board is directed in fixing a need rate to award mail pay in an amount which, when added to all the carrier's other revenue, will provide it with funds necessary to carry out the national air transportation policy. Cf. *Pan American Airways v. Civil Aeronautics Board*, 84 U. S. App. D. C. 96, 97, 171 F. 2d 139, 140.²²

There is nothing in the Act to support the Board's view that it may disregard a portion of such other revenue because of economic policy considerations. The term "all other revenue" in the Act does not mean "all or some part of other revenue." The extent of the carrier's need—

²¹ The Board stated at another point in its opinion (J.A. 55) that it was not deciding whether it had the power to make the offset. We submit that it plainly had the power and the duty to do so.

It should be noted that there is no issue here of the Board's power retroactively to reduce final future rates, as was the situation in *Transcontinental and Western Air, Inc. v. Civil Aeronautics Board*, 336 U.S. 601. In the *Transcontinental and Western* case, the Court held that the Board had no power to fix new rates retroactively for a period during which a final rate previously established was in effect and unchallenged by the initiation of a mail rate proceeding. In the instant case, however, there is no question of retroactively reducing C & S's domestic mail pay previously received under a final rate. C & S fully retains all payments had under that rate. The sole question here is whether the Board was empowered to treat excess profits under such rate as non-existent in determining the carrier's subsidy need on its foreign routes. Certainly C & S cannot claim, by virtue of the *Transcontinental and Western* case or otherwise, any right to have such profits disregarded by the Board when subsidy rates for another segment of its operation are fixed. As shown in Points I and II, *supra*, the Board cannot award mail pay subsidy in excess of the need of the carrier as a whole.

²² This Court there stated: "It has developed in some cases that the carrier had no need for mail pay in addition to reasonable compensation for services rendered; but in other cases there was such need, because *all the other revenue* was not sufficient to enable the carrier to meet the objectives of the statute" (emphasis added). And see *Seaboard & Western Airlines v. Civil Aeronautics Board*, 86 U.S. App. D.C. 64, 68, 181 F. 2d 515, 519, certiorari denied 339 U.S. 963.

and we reemphasize that it is the need of the carrier as a whole²³—is wholly unaffected by the source of the other revenue which the Act requires to be offset.

If a statute provided that in fixing the rates of a public utility a regulatory Commission was to take into account all of the utility's plant and property dedicated to the public service, it could hardly be suggested that the agency might "consider" a particular facility and determine that it was so dedicated, but nevertheless elect to exclude it from the rate base. No more can the Board determine that certain income constitutes other revenue, and then "consider" such other revenue in a manner which effectively eliminates it from the final computation of the carrier's need for subsidy.

The requirement of the Civil Aeronautics Act that "all other revenue" is to be offset in determining a carrier's subsidy need reflects an important public policy. Clearly, the carrier does not "need" subsidy if its "other revenue" is sufficient to enable it "to maintain and continue the development of air transportation." To whatever extent the carrier has sufficient "other revenue" to enable it to meet that objective in part, its "need" for subsidy is *pro tanto* diminished. Congress, which recently has shown great concern for the huge subsidies the airlines have received from the public treasury,²⁴ clearly manifested an intent to keep subsidies to a minimum when it adopted the strict "need" standard of Section 406(b).

A statute providing for government subsidy of private enterprise should be construed so as to give effect to the limits prescribed by Congress, which presumably were fixed to safeguard against unwarranted payment of public funds. The Supreme Court has repeatedly pointed out

²³ See *supra*, pp. 10-12.

²⁴ Separation of Air-Mail Pay From Subsidy, Committee Print, May 5, 1950; S. Rep. No. 629, 82d Cong. 1st Sess. (1951).

The Board has estimated that \$270,000,000 of the \$457,000,000 mail pay received by domestic carriers from the passage of the Act in 1938 to June 30, 1951, or almost 60%, represents subsidy. Civil Aeronautics Board, Administrative Separation of Subsidy from Total Mail Payments to Domestic Air Carriers, September 1951, p. 5.

that statutory grants of public property to private individuals are to be strictly construed.²⁵

The Board's treatment of the "all other revenue" clause in Section 406(b) could lead to emasculation of the entire need standard. The same type of "economic policy considerations"²⁶ relied upon by the Board to justify fixing

²⁵ *Slidell v. Grandjean*, 111 U. S. 412, 437; *Central Transportation Co. v. Pullman's Palace Car Co.*, 139 U. S. 24, 49; *Northern Pacific Railway Company v. Soderberg*, 188 U. S. 526, 534; *Northern Pacific Railway Co. v. United States*, 330 U. S. 248, 257.

The Comptroller General recently held that the Federal Airport Act, 60 Stat. 170, 49 U.S.C. 1101 *et seq.*, which authorizes the Civil Aeronautics Administrator to grant federal funds for "airport development," does not empower the Administrator to grant funds to build a civic auditorium and adapt a fire prevention reservoir as a swimming pool at a local airport, even though such facilities would "indirectly promote aviation" by centering community interest in the airport. Comp. Gen. Dec. B-108691, June 4, 1952, 20 Law Week 2600 (June 17, 1952).

²⁶ Since we contend that Section 406(b) requires the Board to offset all of the carrier's other revenue in determining its subsidy need, we deem such "economic policy considerations" irrelevant in fixing subsidy mail pay. We note in passing, however, that if such considerations were material, the ones relied upon by the Board in this case plainly would not justify refusal to make the offset.

The Board's final opinion relies upon two principal economic factors. First, it is suggested that the "more robust" domestic segment of the industry should not be burdened with the obligations of the "economically weaker" international segment (J.A. 54). There are several answers to this. Although this consideration might justify a higher rate of return for international than for domestic operations—as the Board in fact provides—it cannot justify giving a carrier a subsidy in excess of its need. Nor is it clear how the domestic segment of the industry would be prejudiced by application of "excess" profits against a carrier's need on its foreign routes. While this rationale might justify preservation of a carrier's domestic earnings up to a "fair and reasonable" level, it cannot be applied to excess earnings realized through subsidy pay from the public treasury. A carrier on a need rate cannot complain if excess earnings are used to meet its requirements on other segments of its system. If this carrier were not receiving subsidy mail pay, the normal course of business would require its profitable routes to absorb operating losses on less profitable segments. It should not be in any better position by virtue of the fact that its risks of loss are minimized by subsidy payments from the public treasury.

It must be borne in mind that C & S had "excess" profits for 1948-1950 only by virtue of the substantial subsidy it received for those years. The estimated amount of the carrier's domestic subsidy during those years—roughly \$4,500,000—is set forth in Appendix A.

The second factor relied on by the Board is the desirability of maintaining the comparative status between domestic carriers which have foreign routes and those which do not. The Board suggests that elimination of such status would handicap it in fixing class rates, although it does not indicate how

independent rates for domestic and international operations, without regard to each other, might also be said to justify awarding domestic need mail pay for particular divisions or even routes. Carried to its logical conclusion, the Board's approach would justify it in setting separate "need" rates for those routes which operate at a loss, without regard to the carrier's overall favorable financial position.²⁷ That was not the basis upon which Congress contemplated that subsidy mail pay would be given when it directed in Section 406(b) that such subsidy was to be awarded in an amount which, together with all other revenue, would meet "the need of each such air carrier."

offsetting excess earnings would have that effect. However, as pointed out *supra*, page 12, we do not challenge the Board's power to fix separately domestic and foreign rates. Nor do we contest the Board's practice of fixing class rates—a practice employed only for carriers on a service rate. Our sole attack is on the Board's refusal to offset excess domestic earnings in determining a carrier's subsidy need on its international division. The offsetting of such excess earnings would in no way preclude continued utilization of the comparison technique of rate making.

In any event, we submit that the policy considerations relied on by the Board could not possibly justify a finding—which the Board did not make—that C & S needed the additional \$654,000 within the meaning of Section 406(b).

²⁷ That such a possibility is not mere conjecture for purposes of argument is suggested by the situation that confronted the Board in fixing mail pay for Mid-Continent Airlines. Mid-Continent, a trunkline carrier, was temporarily certificated for a feeder route, which the Board required the carrier to treat as a separate entity for accounting purposes. *Parks Investigation Case*, Docket No. 3965, et al., Order No. E-4472, July 28, 1950, mimeographed pp. 25, 28. Subsequently the Board, in awarding temporary mail pay covering the feeder route, expressly provided that if the earnings from the rest of the carrier's operations exceeded a fair and reasonable return, "the excess may be offset against the mail pay need determined in the final mail rate proceeding" for the feeder route. *Mid-Continent Airlines, Mail Rates*, Docket No. 4680, Order No. E-4938, December 14, 1950. Although the Board there contemplated making the offset, economic policy considerations might, under the Board's theory in the instant case, dictate against the offset in some other similar situation.

CONCLUSION

For the foregoing reasons the order of the Board should be modified to reduce C&S's mail pay in the amount of \$654,000.

Respectfully submitted,

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JULY, 1952

APPENDIX A

Chicago and Southern—Domestic Services

REPORTED	1948	1949	1950	1948-1950 total
U. S. mail revenues received	\$1,891,989 ¹	\$1,800,384 ¹	\$1,747,319 ²	\$5,439,692
U. S. mail ton miles of traffic	481,731 ³	520,462 ³	608,040 ⁴	
U. S. mail revenues per ton-mile of U. S. mail	\$3.92 ¹	\$3.45 ¹	\$2.87 ²	
COMPUTATIONS				
If a mail service ton mile rate of	\$0.53 ⁵	\$0.53 ⁵	\$0.53 ⁵	
were applied, the resulting mail revenues would be:	\$255,317	\$275,845	\$322,261	\$853,423
Subsidy estimated by subtracting revenues computed on 53¢ ton mile rate basis from mail revenues actually received	\$1,636,672	\$1,524,539	\$1,425,058	\$4,586,269

Source:

¹ C.A.B. Recurrent Reports of Financial Data, C & S (Domestic Services), 4th Quarter of 1949.

² C.A.B. Recurrent Reports of Financial Data, Domestic Air Mail Carriers, Trunk Lines, 12 months ended 12-31-50, page 2 of 4.

³ C.A.B. Recurrent Report of Mileage & Traffic Data, C & S (Domestic Services), 4th Quarter 1949.

⁴ C.A.B. Recurrent Report of Mileage & Traffic Data, Domestic Air Mail Carriers, Trunk Lines, 12 months ended 12-31-50, page 2 of 4.

⁵ This 53¢ per ton mail rate was utilized by the Board in calculating C & S's subsidy in its Report on Administrative Separation of Subsidy from Total Mail Payments to Domestic Air Carriers, *supra*, note 15, and was applied by the Board in separating the carrier's service mail pay from subsidy. *Chicago and Southern Airlines, Domestic Operations*, Docket No. 5144, Order No. E-5869, November 15, 1951. There the Board, in fixing prospective annual mail pay of \$1,045,000, stated that \$382,000 represented service mail pay at 53¢ per ton mile, "and the balance of \$663,000 is subsidy." (*Id.* at mimeographed p. 7).

BRIEF FOR RESPONDENT

United States Court of Appeals
for the District of Columbia Circuit

No. 11,351

FILED SEP 26 1952

Joseph W. Stewart

JESSE M. DONALDSON, POSTMASTER GENERAL OF THE UNITED
STATES, AND THE UNITED STATES OF AMERICA, ON BE-
HALF OF THE POSTMASTER GENERAL, *Petitioners,*

v.

CIVIL AERONAUTICS BOARD, *Respondent.*

On Petition for Review of Orders of the Civil Aeronautics Board

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COUNTERSTATEMENT OF QUESTIONS PRESENTED

In respondent's view, the questions presented by this case are

1. Whether, after having established C. & S.'s domestic and international divisions as separate units for rate-making purposes and after having fixed a final rate for the domestic division in advance of the other, the Board had authority to subsequently refuse to offset the profits accruing under the final domestic rate against the carrier's need for mail pay for the international division, and, if so,

2. Whether the Board abused its discretion in refusing to offset the profits from the domestic division against C. & S.'s need for mail pay for its international division.

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United States Court of Appeals for the District of Columbia Circuit

No. 11,351

JESSE M. DONALDSON, POSTMASTER GENERAL OF THE UNITED STATES, AND THE UNITED STATES OF AMERICA, ON BEHALF OF THE POSTMASTER GENERAL, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

On Petition for Review of Orders of the Civil Aeronautics Board

BRIEF FOR RESPONDENT

COUNTERSTATEMENT OF THE CASE

The Postmaster General seeks review in this case of an order entered by the Civil Aeronautics Board fixing mail pay for the international operations of Chicago and Southern Air Lines, Inc. (C. & S.) (J.A. 51). The single issue presented is whether the Board erred in refusing to reduce the allowance for mail pay for international operations by approximately \$654,000, the amount of "excess" profits which had accrued to C. & S. under a final mail rate for its domestic operations.

C. & S. conducts domestic operations over routes extending between Chicago and Detroit, on the one hand, and

Houston and New Orleans, on the other, and international operations over routes extending between Houston-New Orleans and Caracas, Venezuela via Havana and Kingston (See 9 C.A.B. 786, 789, 790, J.A. 7). The certificates of public convenience and necessity for both operations authorize the transportation of mail, and the carrier is entitled to compensation therefor at rates fixed by the Board pursuant to the provisions of Section 406 of the Civil Aeronautics Act (52 Stat. 998, 49 U.S.C. 486). These provisions authorize the fixing of "need" or subsidy mail rates for air carriers, and C. & S. was a "need" or subsidized carrier as to both its domestic and international operations at all times material to this case. Further, as is customary where a single carrier conducts both domestic and international operations of substantial size, different rates were prescribed by the Board for C. & S.'s domestic and international operations, and these rates were fixed in different proceedings before the Board.

C. & S.'s first international operations were inaugurated in 1946 (J.A. 8). At that time, the domestic operations were being conducted under provisional or temporary rates (See 9 C.A.B. 786, 789, 790). A temporary rate also was fixed early in 1947 for the international operations then being conducted (J.A. 8). On July 28, 1948, the Board established a final need rate for the domestic operations to be effective on and after January 1, 1948. *Chicago and Southern A. L., Mail Rates*, 9 C.A.B. 786 (1948). That order continued in effect at all times material to this case, and no petition for a new domestic rate had been filed either by the carrier or the Postmaster General. International operations continued under temporary rate orders until the entry of the order which is the subject of this review proceeding.

The order under review (J.A. 51) fixed final rates for the international operations for the past period November 1, 1946-December 15, 1950, and for the future period beginning December 16, 1950 (J.A. 59). For the past period, the one principally in issue, the Board determined the carrier's international "break-even need" (the amount neces-

sary to equalize income and outgo recognized for mail pay purposes) to be \$3,122,000 (J.A. 19). Return on investment at the rate of 7% was allowed in the amount of \$393,000 (J.A. 23). Actual income tax liability for the past period was determined to be \$147,000 and this amount allowed (J.A. 57). Thus, total mail pay for the past period was granted in the amount of \$3,662,000 (J.A. 58).

The Postmaster General contended before the Board, and contends here, that the mail pay allowance for the international operations should have been reduced by \$654,000. This sum represents the profits earned for the period 1948-1950 under the final rate for the domestic system in excess of a 7.4% return on investment. The domestic rate had been fixed at a level which would afford the carrier an opportunity to earn approximately 8% on investment under normal operating conditions, and the estimated rate of return on the basis of the carrier's predictions of future traffic had been 7.4%. *Chicago and Southern A. L., Mail Rates*, 9 C.A.B. 786, 812 (1948).¹ The domestic earnings or profits in excess of 7.4% were considered by the Postmaster General to constitute "other revenue" to the carrier to be taken into account in determining the amount of international mail pay which should be allowed, and, according to him, the Board mandatorily was required to offset these profits against the carrier's "need" for mail pay for the international operations.² The Board attorney assigned to the case was of the view that the offsetting of these earnings would constitute a forbidden recapture of earnings accrued under a final rate (J.A. 53). Without passing on the ques-

¹ Actually the domestic rate fixed in 1948 was a "sliding scale" rate designed to yield a higher return with increasing load factors, and the sliding scale was such that the carrier might either have lost money, or have realized a return on investment in excess of 13%, depending on load factors. Moreover, the Board advised C. & S. in fixing the rate that any economies in operations which might be achieved would "inure to the carrier in the form of higher earnings" (9 C.A.B. at p. 812). C. & S. in fact achieved operating economies. This factor, together with various accounting adjustments made in the depreciation account to reflect subsequent changes in the service life of DC-3 and DC-4 aircraft, resulted in a rate of return on investment for the period 1948-50 of 12.51% (J.A. 65).

² Section 406(b) (52 Stat. 998, 49 U.S.C. 486(b)) provides in part that, in fixing mail rates the Board shall consider, among other factors, the "need" of the carrier for subsidy mail pay in the light of "all other revenue of the air carrier."

tion of its power to make the offset (J.A. 21, 55), the Board held that in any event (J.A. 54)

. . . while we are required to take into consideration the need of a carrier for mail compensation together with "all other revenue", we believe that we are not required by Section 406(b) to reduce the carrier's mail pay with any part of such other revenue if there are sound reasons for not doing so as a matter of economic policy.

The Board concluded that as a matter of policy the offset contended for by the Postmaster General should not be made.

The Board explained the necessity and desirability for neither recapturing profits nor making up losses resulting from final divisional rates and of otherwise maintaining domestic and international operating divisions as separate rate-making units in appropriate cases, both for achieving the purposes of the Act and aiding the Board in the discharge of its duties. The Board stated that the statutory goal of a self-sufficient air transportation system can best be achieved by placing carriers on permanent rates under which the carriers will either retain the advantages of good earnings or bear any losses which may occur (J.A. 20). Final rates for both domestic and international operations cannot always be fixed simultaneously, as was true in this case. In such cases, the benefits which flow from placing carriers on final rates are such as to require the fixing of a permanent rate for one division in advance of the other, rather than retaining the carrier on temporary or open rates until such time as rates can be fixed simultaneously for both divisions (J.A. 20, 21). The Board also found that it is desirable to maintain the domestic comparative status between the domestic operators which have foreign routes and those which do not have foreign routes. Since carriers fall into fairly well-defined classes for domestic operations, the Board is enabled to fix uniform domestic mail rates for groups of carriers by excluding consideration of international operations. Such classification and comparative status provide a competitive incentive for

efficient operations, and also permit the Board to use comparative techniques in fixing rates (J.A. 54, 55).

Further, the Board stated that it is reluctant to burden the more "robust" domestic operations with the obligations of the "economically weaker" international operations of carriers engaged in both domestic and international operations, a burdening which will thwart the progress of the domestic operators toward self-sufficiency (J.A. 54). Keeping the domestic industry in a financially sound position will, the Board found, ultimately benefit the public in the form of lower fares, reduced mail compensation, more modern aircraft and improved operating methods (J.A. 54).

STATUTE INVOLVED

Pertinent provisions of the Civil Aeronautics Act of 1938, 52 Stat. 973, as amended, 49 U.S.C. 401 *et seq.*, relating to mail rates are set forth on pages 4 and 5 of the Postmaster General's brief. Other pertinent portions of the Act are cited or quoted at their appropriate place in the text of this brief.

SUMMARY OF ARGUMENT

I

Where domestic and international operating divisions of the same air carrier are established as separate rate-making units and a final rate established for one division in advance of the other, the Board is not thereafter mandatorily required to off-set profits accruing under the final rate against the carrier's minimum need for mail pay for the other division. Section 406(b) of the Act does not limit either subsidy payments or a carrier's "need" for subsidy to that minimum amount necessary to maintain an entire existing air carrier system as the Postmaster General erroneously contends. A carrier's "need" is merely one of several unweighted factors which the Board may consider in fixing mail rates. Further, the term "need" as employed in Section 406(b) expressly includes not only that amount of subsidy necessary to "maintain" a given operation but also that amount necessary to "continue the development

of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service and the national defense." The statutory concept of "need" thus embraces the extent of subsidy required to accomplish these developmental objectives.

II

Maximum operating efficiency and economy on the part of air carriers, and the development of air transportation, is promoted by placing and retaining the carriers on final mail rates under which the carriers either reap the benefits or stand the losses from future operations. Where carriers are comprised of both domestic and international divisions, final rates cannot always be fixed simultaneously for both divisions. In such cases, the benefits which flow from final rates are such as to require the fixing of a final rate for one division in advance of the other, and to justify a subsequent refusal to either offset profits or make up losses between the divisions, even though a carrier may on occasion obtain profits which otherwise would not inure to it. Moreover, the burdening of domestic operations with losses resulting from economically weaker international operations impedes the development of a sound air transportation system, and the maximum benefits which flow from the classifications of carriers established by the Board cannot be obtained unless international and domestic operations are retained as separate rate-making units in appropriate cases.

ARGUMENT

- I. **Where Domestic and International Divisions of the Same Carrier Are Established as Separate Units for Rate-Making Purposes, the Board Has Discretionary Power to Refuse to Offset Profits Accruing From One Division Against the Carrier's Need for Mail Pay for the Other Division.**

In fixing mail rates for C. & S.'s operations and in refusing to offset profits from the domestic operations against the carrier's need for mail pay for the international operations, the Board adopted and gave effect to the familiar rate-making principle of establishing different op-

erating divisions of a carrier as separate units for rate-making purposes. The Postmaster General does not question the Board's power in appropriate cases to fix rates separately and at different times for different operating divisions of a single carrier (Br. p. 12), nor could he in view of the specific statutory authority conferred upon the Board in this respect and in the light of applicable case law.³ Neither does he raise any issue as to the reasonableness of the Board's action in establishing C. & S.'s international and domestic divisions as separate rate-making units and in fixing final rates for one division in advance of the other. Rather, the contention made on his behalf is that profits from one operating division mandatorily are required to be offset against need for mail pay for the other, and that the Board cannot lawfully award subsidy mail pay on a divisional basis for any given period of time in an amount which exceeds minimum operating need for the entire air carrier system during the period, irrespective of whether the operating divisions are established as

³ Section 416(a) of the Act (52 Stat. 1004, 49 U.S.C. 496(a)) empowers the Board to establish classifications of carriers according to the "nature of the services performed", and Section 406 authorizes the fixing "from time to time" of "different [mail] rates for different air carriers or classes of air carriers, and different classes of service." And apart from express statutory authority therefor, the determination of the proper unit for rate-making purposes is a matter committed primarily to administrative discretion. See e.g., *American Toll Bridge Co. v. Railroad Commission of California*, 307 U.S. 486, 494 (1939); *Illinois Commerce Commission v. United States*, 292 U.S. 474, 486 (1934); *Wabash Valley Electric Co. v. Young*, 287 U.S. 488 (1933); *Gilchrist v. Interborough Co.*, 279 U.S. 159, 209-210 (1929).

The Board has recently summarized its criteria for determining whether domestic and international operations shall be regarded as separate units or as a single unit for rate-making purposes as follows (*National Airlines Mail Rate*, Order Serial No. E-6344, dated April 21, 1952):

"There have been various criteria developed to guide the Board's determination of whether a single rate should be set for the foreign operations of a domestic carrier. One is the size of the foreign operation in relation to the total operations of the given carrier; another, the absolute size of the foreign operations; and a third, the extent to which the foreign operations are integrated with the domestic. To establish grounds for separate treatment it must be demonstrated that the foreign operations are large relative to the domestic operations of the carrier; that the foreign operations are so large that it would be neither practical nor feasible to attempt to set a system rate; and that the domestic and foreign operations are carried on more or less independently of each other."

C. & S.'s domestic and international operations are conducted by separate operating divisions and otherwise are such as to warrant their being treated as separate for rate-making purposes.

separate rate-making units or whether the profits involved accrued under a final or temporary rate order.⁴

The Board did not concern itself with the questions of whether the offsetting of C. & S.'s domestic profits would have constituted a forbidden recapture of profits accruing under a final unchallenged rate order, or whether after having elected to treat C. & S.'s divisions as separate rate-making units it lacked authority to offset profits and losses between them without first classifying the entire system as a single rate-making unit.⁵ Rather, the Board adhered to its practice of neither recapturing profits nor making up losses resulting from final divisional rates, upon findings that this practice and that of otherwise maintaining domestic and international operating divisions as separate for rate-making purposes is necessary to accomplish the purposes of the Act, and that the Board has discretionary authority to administer the mail pay provisions in such manner as to best develop a sound air transportation system even though that administration on occasion may require the allowance of subsidy mail pay in excess of mini-

⁴ The term "minimum operating need" as used in this brief refers to the Postmaster General's concept that subsidy mail rates for past periods must be limited to that amount necessary to meet operating expenses and to allow the customary rate of return on investment, and for future periods to a level which will afford the carrier a reasonable opportunity to earn no more than this amount.

⁵ In *Transcontinental & Western Air v. Civil Aeronautics Board*, 83 App. D.C. 358, 169 F. 2d 893 (1938), aff'd 336 U.S. 601 (1949), it was held that the Board lacked authority to fix rates retroactively to include a period in which a final rate was in effect and unchallenged, a course of procedure which the Board consistently had refused to follow on policy grounds. In that case, TWA's domestic operations were on final rates, whereas international operations were being conducted under temporary rates. TWA contended before the Board (J.A. in Case No. 9763, pp. 47, 48 and 89, 8 C.A.B. 685, 702, 703) and before this Court (TWA's brief in Case No. 9763, p. 22) that, irrespective of whether the Board otherwise had power to reopen the domestic rate for the past period, it nevertheless had power to reopen a part of the past period since *system* rates could be fixed from the beginning of international operations in that the Board is empowered to revise mail rates for an entire system retroactively to the time that any part of the system is on an open rate. This contention was rejected by the Board upon the basis that TWA's domestic and international operations were "separate units for rate-making purposes." 8 C.A.B. at p. 703. The Court affirmed the Board's action.

Had C. & S. sustained losses under the final domestic rate, an exact parallel to the TWA case would have been presented, and the Board would have lacked power to make up those losses in fixing the mail rate for the international operations. The question of whether a different rule prevails in the case of profits accruing under a final divisional rate, as the Postmaster General contends (Br. p. 14, n. 21), is irrelevant to the basis of the Board's decision in this case.

minimum operating need.⁶ The Board clearly has such discretionary authority.

Section 406(b) does not limit subsidy payments to that minimum amount required to maintain an existing air carrier system, nor, as we demonstrate hereinafter, is the

⁶ Contrary to the Postmaster General's assertions (Br. p. 11) the Board's refusal to make the offset contended for did not represent a departure from prior Board precedents. It is true that the Board has stated in prior cases that "need" refers to the air carrier as a whole and not to geographical divisions. But these decisions did not purport to define "need" or to pass upon the question of whether mail pay could be awarded in excess of minimum operating need. Moreover, the cases relied upon by the Postmaster General dealt for the most part with the questions of whether, in rate cases where the entire system was the rate-making unit, mail pay could be allowed for all operations rather than being restricted to those schedules and routes over which mail was transported, or whether different rates should be fixed for the different routes which collectively made up the system rate-making unit. In these cases, the Board held that mail pay could be allowed in an amount sufficient to sustain the entire operation, and that different rates should not be fixed for different routes. *Chicago and Southern Air Lines, Mail Rates*, 3 C.A.B. 161 (1941); *Delta Air Corporation, Mail Rates*, 3 C.A.B. 261 (1942); *Eastern Air Lines, Mail Rates*, 3 C.A.B. 733 (1942); *Pennsylvania Central Airlines, Mail Rates*, 4 C.A.B. 22 (1942).

Although fixing mail rates on a system basis wherever possible, the Board nevertheless has heretofore treated foreign and international divisions as separate entities for rate-making purposes in appropriate cases. Further, it has made specific pronouncements with respect to the problem herein involved in two earlier cases. In the case of the domestic and international divisions of TWA, it held that "TWA's domestic and international operations are separate units for rate-making purposes" and that it lacked power to make up TWA's large losses under a final domestic rate in fixing rates for its international operations. *Pennsylvania Cent. Air Et Al. Motions*, 8 C.A.B. 685, 703 (1947), *aff'd Transcontinental & Western Air v. Civil Aeronautics Board*, 83 App. D.C. 358, 169 F. 2d 893 (1948); 336 U.S. 601 (1949). In *Pan American Airways, Latin-American Rate Case*, 3 C.A.B. 657 (1942), the Board determined that Pan American's mail rates for its Latin American Division had resulted in excess profits during the period between the institution of the rate proceeding and its decision therein. Rather than requiring a refund from the carrier, which it clearly could have done, the Board refused to recapture these profits upon "economic considerations and considerations of policy" (3 C.A.B. at p. 668). However, repeating its statement in the *Chicago and Southern Case, supra*, that "need" embraced the needs of the air carrier system rather than geographical divisions, it stated that it would take these excess profits into account in determining the carrier's "need" for mail pay for its other divisions. The proceeding was reopened on reconsideration (6 C.A.B. 85), and final rates fixed simultaneously for all of Pan American's divisions (6 C.A.B. 59, 61, 83, 85). No additional subsidy payments were made since the excess payments for the Latin-American Division which were subject to recapture were more than enough to meet the carrier's "need" for all of its divisions. 6 C.A.B. at p. 78.

The *TWA* case and the instant case demonstrate that where a final rate is established for one division in advance of the other, the Board will neither make up losses nor offset profits resulting from the final division rate. The *Pan American* case demonstrates that, where excess payments made under temporary rates are discovered in advance of or simultaneously with the fixing of a final rate for another division, the Board may require the carrier to offset these excess payments against its "need" for the other divisions rather than itself recapturing the excess payments and then directly making up the "need" for the other divisions.

statutory concept of "need" so limited.⁷ But even if the Postmaster General is correct in his interpretation of need, Section 406(b) plainly provides that need is merely one unweighted factor to be taken "into consideration, among other factors," in fixing mail rates. The other factors which may be taken into account obviously include the overall developmental responsibilities placed upon the Board.⁸ In this view of the case, the situation here presented is similar to and should be controlled by *Secretary of Agriculture v. Central Roig Refining Co.*, 338 U. S. 604 (1950). There the Secretary was directed and empowered to make a determination of sugar quotas upon consideration of three named but Congressionally unweighted factors. The Secretary "considered" all three factors, just as

⁷ Section 406(b) (52 Stat. 988, 49 U.S.C. 486) provides in pertinent part:

"In determining the rate in each case, the Board shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."

⁸ The Congressional mandate of policy contained in the Act (Section 2, 52 Stat. 980, 49 U.S.C. 402) provides:

"In the exercise and performance of its powers and duties under this Act, the Board shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity—

(a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriers.

(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

(d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(e) The regulation of air commerce in such manner as to best promote its development and safety; and

(f) The encouragement and development of civil aeronautics."

the Board considered in this case whether it should offset the domestic profits against C. & S.'s international need, but concluded that one factor should not be applied and therefore should not be given weight. In sustaining the Secretary's action, the Court stated (338 U. S. at pp. 611, 612):

. . . he is under a duty merely to take "into consideration" the particularized factors. The Secretary cannot be heedless of these factors in the sense, for instance, of refusing to hear relevant evidence bearing on them. But Congress did not think it was feasible to bind the Secretary as to the part his "consideration" of these three factors should play in his final judgment—what weight each should be given or whether in a particular situation all three factors must play a quantitative share in his computation.

Moreover, the statutory concept of need is not limited to that amount of subsidy necessary to maintain operations over a given air carrier system. On the contrary, the term need as employed in Section 406(b) expressly includes not only that amount of subsidy necessary to "maintain" a given operation, but also that amount necessary to "continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense." The extent of a carrier's need thus is the extent of subsidy required to accomplish these developmental objectives on either a divisional or system basis, and the powers conferred in administering the mail pay provisions of the Act obviously were designed and intended to be co-extensive with the overall developmental responsibilities placed upon the Board. Due regard for the developmental directives contained in the Act has been recognized by the Court to be "peremptory" upon the Board in certificate cases,⁹ and should be recognized as being equally peremptory in mail rate cases.

The Board has always considered that it has statutory authority, as it does, to allow subsidy mail pay in excess of minimum operating need where reasons of economic

⁹ *American Airlines v. Civil Aeronautics Board*, — App. —, 192 F. 2d 417, 420 (1951).

policy require that action for the furtherance of the statutory goal of a sound and economically self-sufficient air transportation system. Thus, the Board has long employed "sliding-scale" need mail rates which have the effect of yielding a higher return on investment with increasing load factors or decreasing costs, thereby encouraging and rewarding carriers for efficient promotional activity and efficient operations. The Board has refused in several past instances to require carriers to refund mail payments which clearly were subject to recapture because the refunding of those payments would impede the progress of the carrier toward the goal of economic self-sufficiency. *Pan American-Grace Airways, Mail Rates*, 3 C.A.B. 550, 564 (1942); *Pan American Airways, Latin American Rate Case*, 3 C.A.B. 657, 668 (1942); *American Airlines, Mail Rate Proceeding*, 3 C.A.B. 770, 776 (1942). The Board also has refused to offset against a carriers' "need" a portion of the profits derived from a route transfer for the purpose of encouraging other voluntary route transfers required for the development of a sound air transportation pattern. *Western Air Lines, Mail Rates*, Order Serial No. E-5467, dated June 26, 1951.¹⁰

Further, the Board is empowered by Section 406 to fix uniform rates for "classes of air carriers, and different classes of service." This power, recognized by the Supreme Court as an important regulatory device for securing the benefits of competition (*Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601, 606-7 (1949)), cannot be effectively exercised unless the Board is permitted to continue its practice of treating domestic and international operations as separate rate-making units. Further, under any given class rate, some carriers obviously will receive less than their operating needs, whereas others will receive more. In such cases, it might be cheaper to the government to pay each carrier strictly according to its own operating need but it can hardly be argued that the Board is required to subjugate the develop-

¹⁰ This order is presently under review in *Donaldson, et al. v. Civil Aeronautics Board*, U.S. App. D.C., Case No. 11,259.

ment of a sound air transportation system through traditional competitive concepts to this factor.

Thus, the entire purpose and focus of "need" payments are not simply to make a carrier financially whole in the usual sense, but to develop an air transportation system to serve paramount national interests. The Board's refusal to make the offset contended for by the Postmaster General must be evaluated in the light of the meaningful purpose of the mail pay provisions of the Act. If the Board is to accomplish its objectives, it cannot administer those provisions in the manner of a public relief law.

II. The Board Did Not Abuse Its Discretion in Refusing to Offset the Profits From C. & S.'s Domestic Division Against the Carrier's Need for Mail Pay for Its International Division.

Maximum operating efficiency and economy on the part of air carriers obviously is promoted by placing and retaining them on final mail rates under which the carriers either reap the benefits or stand the losses from future operations, irrespective of whether those final rates are "need" or "service" rates. Moreover, the Act contemplates that wherever possible carriers shall be required to operate under such final rates rather than on a cost-plus basis. *Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601 (1949). Because of differing conditions existing in the domestic and international field, it is not always feasible for the Board to fix a single mail rate for carriers comprised of domestic and international operating divisions, and separate final rates often may be established for one division in advance of the other (J.A. 20). In cases which involve need rates for both divisions, the Board either may retain the carrier on a temporary rate or "cost-plus" basis as to its entire operations until such time as final rates may be fixed simultaneously for both divisions, thereby avoiding the problem of offsetting profits here involved, or it may fix a final rate for one division in advance of the other for the purposes of obtaining the benefits which result from final rates to the greatest extent practicable, even though the carrier as a result of that action

may obtain mail pay which otherwise would not inure to it.¹¹

The Board reasonably has elected in such cases, as in this case, to follow the second alternative, not only because of the benefits which flow from placing carriers on final rates but also because of the overall desirability for maintaining domestic and international operating divisions as separate rate-making units in appropriate cases. The reasonableness of the Board's policy in this latter respect is best demonstrated against the background of the situation existing with respect to carriers engaged in both domestic and international operations.

Four of the fourteen domestic trunk lines (TWA, Braniff, C. & S. and Northwest) presently are engaged in both domestic and international operations which are classified as separate units for rate-making purposes.¹² Of these four, all but C. & S. are paid at compensatory rates for domestic operations. Domestically, TWA is classified with American, Eastern, and United as the "Big Four" carriers paid at the lowest service mail rate for domestic operations, presently 45 cents per ton-mile. Braniff and Northwest are classified for domestic operations with four other domestic carriers (Capital, Delta, National and Western) as falling within the group of carriers paid at a service rate of 53 cents per ton-mile. C. & S. also has been classified by the

¹¹ We recognize that under the Postmaster General's views a third alternative is presented, that of fixing a final rate for one division in advance of the other and placing the risks of future losses on the carrier but at the same time retaining for the benefit of the government the advantages of any possible future profits. Whatever may be the legal power of the Board in this respect, it has not yet chosen to follow this possible third alternative. Moreover, it is apparent that this course of action would not provide the same spur to efficient operations as is provided by allowing the carrier to retain the benefits of profitable operations. Indeed, a carrier would have little incentive to achieve economies during the period which intervenes between the fixing of a final rate for one division and a final rate for the other. On the contrary, it would be to the carrier's advantage to conduct its affairs in such manner as to minimize the profits which otherwise would be recaptured.

¹² Five other carriers (American, Eastern, United, National, and Colonial) conduct foreign or overseas operations which in the past have been regarded as separate units for rate-making purposes but which presently are regarded as "stub-end" operations sufficiently integrated with domestic operations so as to make feasible the fixing of rates on a system basis. See C.A.B. publication "Administrative Separation of Subsidy from Total Mail Payments to United States International, Overseas and Territorial Air Carrier," 1952, pp. 7 & 8.

Board as comparable with these six carriers for service mail rate purposes and it is hoped that C. & S. will in the future be placed on a service rate of 53 cents per ton-mile.¹³ Uniform class mail rates as yet have not been established in the international field. Nevertheless, the Board has classified international operations for comparative rate-making purposes. TWA's international operations are classified as comparable to those of Pan American's Atlantic Division and Northwest's with Pan American's Pacific Division. The international operations of C. & S. and Braniff are grouped with those of Panagra.¹⁴

The percentage of subsidy to total mail payments is substantially greater in the international field than in the domestic field, and the Board has estimated that the level of subsidy support for international operations will tend to increase over the next several years.¹⁵ On the other hand, those domestic trunk line operations which still require subsidy support appear to be well on the road to economic self-sufficiency.¹⁶

The Board has heretofore determined that the public interest requires the participation of more than one American flag carrier in the international field. *American Export Air., Transatlantic Service*, 2 C.A.B. 16 (1940); *Northeast Air. Et Al., North Atlantic Routes*, 6 C.A.B. 319 (1945). The selection of domestic carriers to perform international services benefits international operations in that existing experienced headquarters staffs, trained operation crews and workers, and shops for the maintenance and repair of aircraft can be utilized in both operations. *Northeast Air. Et Al., North Atlantic Routes, supra*, 6 C.A.B. at pp. 326-327. The use of these existing facilities, and the spread of

¹³ See C.A.B. Publication "Administrative Separation of Subsidy from Total Mail Payments to Domestic Carriers," 1951, p. 14.

Braniff, C. & S., Northwest, Capital, Delta and Western for many years were classified as the "Little Six" domestic carriers for service mail rate purposes.

¹⁴ See C.A.B. Publication "Administrative Separation of Subsidy from Total Mail Payments to United States International, Overseas and Territorial Air Carriers," 1952, p. 7.

¹⁵ *Ibid*, p. 4.

¹⁶ See C.A.B. Publication "Administrative Separation of Subsidy from Total Mail Payments to Domestic Air Carriers," 1951, p. 7.

overhead costs made possible thereby, often enables both domestic and international operations to be performed more economically by carriers engaged in both types of operations than would be possible if the operations were conducted by entirely separate carriers. Moreover, where consistent with the various other criteria which the Board must consider, the Board will select to operate a given route that carrier which can provide a single-carrier and therefore a more convenient service to the largest portion of the traveling public. *Additional Service to Latin America*, 6 C.A.B. 857, 900 (1946). The certification of domestic carriers for international operations will provide maximum single-carrier service to foreign points in most cases, and C. & S. was certificated for its Latin American routes largely because it could provide a "single-carrier operation connecting the important cities of the Mississippi Valley and the Great Lakes region with points in the Caribbean and on the north coast of South America." *Additional Service to Latin America*, *supra*, 6 C.A.B. at p. 910.

TWA, Braniff, C. & S. and Northwest compete domestically with other trunk line carriers engaged only in domestic operations, many of which either do not require subsidy support or are rapidly approaching that stage. Commercial rates must be maintained for competitive reasons at approximately the same level for the domestic trunk line carriers. Assuming that the domestic fare structure is or could be established at a level which would enable domestic operations to support all or a part of international operations and that the Board should require such support, then carriers engaged in both types of operations obviously would not obtain the same rate of return on investment that wholly domestic carriers would earn. Under these circumstances, domestic carriers would be reluctant to conduct or expand international operations, with a consequent loss of the operating experience and economies and convenient freight, passenger and mail service which they can bring to the international field. Moreover, the Board is of the view that any excess earnings in the domestic field should be used either for improved domestic services, or

as the basis for reducing domestic commercial rates with new impetus to the further development of the industry (J.A. 54), a determination within a field committed to the competence of the Board and entirely reasonable.

Actually, it is unlikely that domestic operations will be able to support international operations in the immediate future. On the contrary, as the Board found, the carrying of international operations on the back of domestic operations would be "subjecting the latter to an unjustifiable strain" and would merely serve to impede the progress of domestic operations toward economic self-sufficiency (J.A. 54). Under these circumstances, and in any event under the Board's view that domestic commercial rates should be fixed at a level necessary to sustain only domestic operations, those carriers engaged in both domestic and international operations presently must be subsidized as to their international operations. The treatment of the entire air carrier system rather than the operating division as the rate-making unit would mean only that these carriers would then be subsidy or need carriers on a system rather than on a divisional basis.

This result would not carry any attendant benefits since the Board's policy of establishing domestic and international operating divisions as separate rate-making units and of fixing final rates for one division in advance of the other need not result in excessive profits to carriers to any greater extent than where carriers are placed on final system rates. Indeed, the Board's policy will result in savings to the government where losses are experienced by a carrier under a final divisional rate. Either excess profits or substantial losses are possible under any final rate, and it is for this reason that rates are not immutable. If a final divisional rate embodies subsidy payments and the profits thereunder prove excessive, then both the Board and the Postmaster General are free to institute proceedings for a lower divisional rate just as in the case of a system rate. Section 406(b).¹⁷

¹⁷ A domestic divisional rate lower than the one here involved subsequently has been established for C. & S. See J.A. 53. The Board maintains constant

The foregoing considerations clearly outweigh the short term benefit which would have resulted from recapturing the sum of money here involved. Further, adoption of the offset principle would have impaired the Board's existing classification system since carriers engaged in both domestic and international operations would then be required to be regarded for many purposes as one air carrier system. This impairment would have precluded the Board from obtaining the maximum benefits which flow from the classifications which it has established, including those of comparative rate-making techniques. The Board did not abuse its discretion in refusing to accede to the principle for which the Postmaster General contends.

CONCLUSION

Upon the basis of the foregoing reasons and authorities, the Board's order should be affirmed.

Respectfully submitted,

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scrutiny over the earnings of carriers under final mail rates, and institutes proceedings for the fixing of lower rates if and when it becomes apparent that the existing rate is too high. Pursuant to this policy, new rate proceedings were instituted by the Board during fiscal year 1952 for the reduction of the mail rates of nine air carriers. Five such proceedings had been instituted during fiscal year 1953 up to the time of the preparation of this brief, including a proceeding for the reduction in the international rate for the future period established for C. & S. in this case.

It is obvious, of course, that a reasonable and representative period of time must elapse before it can be determined whether a particular rate is providing excess earnings since air carrier revenues are subject to the same fluctuations that exist in other fields.

**BRIEF FOR CHICAGO AND SOUTHERN AIR LINES,
INC., INTERVENOR.**

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 11,351

JESSE M. DONALDSON, Postmaster General of the United States, and THE UNITED STATES OF AMERICA on behalf of the Postmaster General, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

**On Petition for Review of Order of the
Civil Aeronautics Board.**

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COUNTERSTATEMENT OF QUESTIONS PRESENTED.

In intervenor's opinion, the questions presented by this case are:

- (1) Does the Civil Aeronautics Board have discretionary authority to establish separate operating units or divisions within a single company for rate-making purposes?
- (2) If the answer to (1) is in the affirmative, and in the exercise of such discretion the Board has in fact separated a carrier's international and domestic divisions for rate-making purposes and has established a final rate for the domestic division in 1948, in establishing the proper rate for the international division in 1951 is the Board legally empowered to offset a portion of the earnings of the domestic division under a final and unchallenged rate against the requirements of the international division?
- (3) If the answer to (2) is in the affirmative, is the Board's power to offset discretionary or mandatory?
- (4) If the answer to (3) is that the power is discretionary, has the Board abused its discretion in refusing to offset in this particular case?

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United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 11,351

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v.

CIVIL AERONAUTICS BOARD, *Respondent*.

On Petition for Review of Order of the
Civil Aeronautics Board.

BRIEF FOR INTERVENOR.

COUNTER-STATEMENT OF THE CASE.

Chicago and Southern Air Lines, Inc., was granted leave to intervene in this proceeding by order of this Court entered April 21, 1952.

The Civil Aeronautics Board, in July of 1948, fixed final mail rates effective January 1, 1948 for the operations of Chicago and Southern Air Lines, Inc. over its domestic routes. When fixing the final domestic mail rates, the

Board established a rate which it estimated would return the carrier a minimum of 7.4 percent on that portion of the carrier's investment properly allocated to its domestic operations. The final rates so established for the domestic division remained in effect and unchallenged during each of the years 1948, 1949 and 1950. The domestic rate after 1950 is not in issue in this case. For the period 1948-1950, the domestic routes of the carrier under the final mail rates prescribed by the Board yielded an average return on investment estimated at 12.5 percent. The Postmaster General contends that the post 1948 earnings over and above the *minimum* return of 7.4 percent estimated by the Board in establishing the domestic mail rate are "excess earnings". This erroneous characterization is inconsistent with the Board's decision in the 1948 *C & S Domestic Mail Rate Case*.¹ In that case the Board specifically held that a 7.4 percent return was not to be considered a ceiling and declared that any economies which the carrier's management succeeded in accomplishing would inure to the carrier in the form of higher earnings.

In an Opinion and Order issued on October 18, 1951 the Board fixed final mail rates for the Latin American operations of Chicago and Southern Air Lines, Inc. The carrier contended in the case before the Board (a) that the Board did not have the power to offset in the international rate case the earnings established three years earlier under the final domestic mail rate, and (b) that even if such power to offset did exist, the Board's power was discretionary rather than mandatory and that sound arguments of economic and regulatory policy argued against the imposition of such an offset. The Board did not rule directly on its legal power to offset but, assuming such a power, held that in the exercise of its discretion it found that sound reasons against offset did in fact exist. The Postmaster General challenges both the carrier and the Board, arguing that under the statute the requirement that the Board offset is

¹ 9 CAB 786 (1948).

mandatory. He contends that under Section 406(b) the Board must, as a matter of law, offset the profits from earlier years derived from the carrier's domestic operations in fixing and determining the rates of compensation for the carrier's transportation of mail over its Latin American routes and had no statutory authority to exercise a discretionary judgment in the matter.

STATUTES INVOLVED.

The pertinent provisions of the Civil Aeronautics Act of 1938, 52 Stat. 977, as amended, 49 U. S. C. 401 *et seq.* are set forth in full in the appendix hereto.

SUMMARY OF ARGUMENT.

I.

The Board is legally empowered to establish separate rate-making units within a single company for rate-making purposes. The Board did not err in determining that C & S' domestic and international divisions constituted two separate rate-making units. As a regulatory agency it is vested with discretion to select an appropriate rate-making unit on a case to case basis. This is so especially where, as here, the carrier rendered two distinct types of service. The treatment of C & S' international division as a rate making entity separate and apart from the domestic division was authorized by the Act. Section 406(b) of the Act expressly authorizes the Board to fix different rates for different classes of carriers after considering the conditions peculiar to that class of air carrier. Section 801 of the Act also recognizes the basic difference between domestic and international air operations. The Board's judgment that each division should stand on its own feet and bear its own burdens was not only authorized but contemplated by the Act.

II.

Aside from the Board's statutory authority to treat C & S' Latin American operation as a separate carrier for rate-making purposes, there exists ample support from a practical policy standpoint. The United States carriers must be given every advantage and opportunity to compete on the same level and under the same conditions with foreign flag air carriers or else the efforts of the United States lines to engage successfully in foreign air transportation would be effectively thwarted. If the domestic service of a United States carrier is to be burdened with the losses of its foreign service, the natural tendency would be for present United States air carriers to discontinue entirely or seriously curtail existing foreign service. It would also discourage other domestic carriers from even entering the foreign field. The Board's judgment in treating the carriers international division as a separate rate-making unit was a fair and reasonable exercise of discretion.

III.

Having established separate international and domestic divisions of C & S for rate-making purposes, and having established final and permanent rates for the domestic division in 1948, the Board is not legally empowered to offset allegedly excessive earnings of the domestic division under the final and unchallenged 1948 domestic rate in establishing proper rates for the international division in 1951.

The offset of such earnings would have the effect of retroactively revising the closed and permanent domestic rate. The Board has no express or implied jurisdiction to revise rates retroactively or to disturb past earnings. An attempt to revise rates retroactively through a policy of offset would prevent air carriers from being placed on permanent rates and would lead to a cost-plus basis of rate-making. The cost-plus basis would not harmonize

with the clear purposes of the Act. It would violate the traditional concepts of rate-making. The language of the Act nowhere suggests that Congress intended to break with the traditions of rate-making.

IV.

If the Board is legally empowered to effect such an offset of domestic profits in establishing proper rates for the international division, the Board's power is discretionary rather than mandatory.

Under Section 406(b) of the Act, the Board is not *required* to offset past earnings but is only *required to consider* such earnings among "other factors" in fixing fair and reasonable rates. The Act vests in the Board the discretionary power to include or not to include "other revenues" where such action in its expert judgment will best effectuate statutory policy. Congress did not limit the Board in fixing fair and reasonable rates to the minimum amount necessary to maintain an existing operation, but empowered the Board to fix a mail rate that would provide for incentive and development of air transportation.

V.

The Board has not abused its discretionary authority in refusing to offset domestic profits of the carrier. On the contrary the conclusion of the Board not to adopt the offset policy was reasonable and proper and fully warranted in view of important economic and policy considerations. The Postmaster General can not quarrel with the Board's objective to place air carriers on self-sufficient basis as rapidly as possible. This objective, in the judgment of the Board, can best be obtained by placing carriers on a permanent mail rate. A policy of offset would unquestionably destroy the permanency of a rate because the carrier would not know from one accounting period to another how much of its earnings it would be allowed to retain. Without a per-

manent rate there would be no incentive to maximum economy and efficiency in airline operations. Permanent rates should be inviolable until adjusted as to future periods through due process after notice and hearing.

If the offset policy were adopted, thus permitting the Board in effect to recapture past earnings on domestic operations under permanent mail rate order, great financial confusion would result. Investors would be misled, ability to attract capital would be impaired, no dividend declaration would be secure and no offering of securities would have a firm foundation.

It would also be contrary to the public interest to burden the robust domestic operation with the economically weaker international operation. The imposition of such burden would postpone indefinitely the desirable objectives of lower fares to the public, the acquisition of new and modern aircraft, the installation of new and modern safety devices, and generally, the attainment of self-sufficiency. Rather than be burdened with unprofitable international operations, the United States domestic carriers would withdraw from the international field to the advantage of the foreign flag carriers and to the detriment of the national defense and the Postal Service.

The adoption of the offset policy is undesirable from an administrative standpoint because it would prevent the Board from preserving a comparative status between domestic operators which have foreign routes as against those which do not have foreign routes. The advantages of the comparative technique of analysis in rate-making are manifold and indispensable. Without it the Board would have no safe guide to chart its course in performing its rate-making functions.

The adoption of the offset policy resulting in a recapture of past earnings over a substantial period of time is contrary to established Board policy and justice and equity forbid confiscation of profits earned under a permanent rate when losses under a permanent rate are not recoverable by the carrier.

VI.

The Court should give great weight to the construction placed upon a statute by an administrative agency charged with the responsibility for the administration and enforcement of the statute. The Board's long record of practical experience with air transportation entitles its judgment to persuasive consideration by the Court. The Board is in a better position than a reviewing Court to determine appropriate applications of a statute which it is directed to administer. The construction of Section 406(b), urged by the Board and the carrier is consistent with the intent of Congress and the language of the Act. It has a reasonable basis in law and should be binding upon this Court in its review of the Board's Order of October 18, 1951.

ARGUMENT.

I.**THE ACT CONFERS DISCRETIONARY POWER ON THE BOARD TO DETERMINE APPROPRIATE UNIT FOR RATE-MAKING PURPOSES.**

The Postmaster General contends that the Board has no authority under the Act to "compartmentalize" the carrier for mail rate purposes. It is well settled that the Board, in common with other regulatory agencies, enjoys primary administrative discretion to determine the appropriate unit for rate-making purposes.

The clear mandate of Section 406(b) of the Act which requires that mail pay shall be awarded in an amount corresponding to the statutory "need" for such compensation as a means of maintaining and continuing the development of air transportation in the public interest will only be met by a determination that C&S domestic and international divisions constitute two separate rate-making units.

The treatment of an international division as a rate-making entity, separate and apart from the treatment of

a domestic division, is both desirable and necessary and is authorized by the Act. The first sentence of Section 406(b) authorizes the Board to fix different rates for different classes of service after considering the conditions peculiar to that class of air carrier. It necessarily follows that if the Board has the power to fix the international division as a separate rate-making unit it could, by virtue of the nature of such power, exclude domestic earnings in establishing international rates in the instant case. The domestic and international divisions of C&S have always been regarded as separate and independent rate-making units because the standards applicable to one are not necessarily applicable to the other.

The Board's administrative interpretation of the Act is in line with the fundamental tenet of public utility law that regulatory agencies are vested with discretion to select an appropriate rate-making unit on a case-to-case basis. C&S is rendering two distinct services—domestic transportation by air and international air transportation. The Latin American air routes are not used or useful to render any service covered by the domestic operations. The carrier's duty to operate either service is independent of its obligation to operate the other.²

Segregation of operations by the same company in fixing rates for separate departments or services of the company has been followed in many rate-making proceedings and upheld by the courts.³

The Michigan Public Service Commission, in an investigation of the rates and charges of the Detroit Edison Company upon a petition of the City of Detroit,⁴ rejected the contention of the company that its steam-heating business was an essential adjunct to its electric business, and that the two services were so interconnected and interdependent that it was impossible to consider the facilities of the

² *American Toll Bridge Company v. Railroad Commission of the State of California*, 307 U. S. 486, 83 L. ed. 1414.

³ *Re Ohio Bell Telephone Co.*, 2 PUR (N. S.) 113, 623.

⁴ *Detroit vs. Detroit Edison Co.*, 59 P. U. R. (N. S.) 1.

two departments separately, and that they should be considered as one integral utility for rate-making. The Commission found that the steam-heating business was separable and that it should be so treated. The Commission said:

"It is a fundamental principle of utility regulation that each type of utility service should be self-sustaining. *It is inequitable to allow the losses of one type of service to become a direct burden upon another type of service.* It does not appear appropriate that the steam heating division of the company should be consolidated with the electric division." (Emphasis supplied).

In *Southwestern Bell Teleph. Co. v. City of San Antonio*, 2 F. Supp. 611, a proceeding involving an alleged confiscatory rate ordinance affecting the City of San Antonio, it was held that the telephone company doing a state and interstate business must segregate its properties, revenues and expenses relating to the city service from those relating to the balance of its services. The Court said that the issue for determination *was not whether the company was earning an adequate net revenue on its entire properties, but whether the rates fixed for local exchange service in San Antonio were sufficient to permit the plaintiff to earn a fair return on its property devoted to the public use within the jurisdiction of the city.*

Where a company renders distinct types of service, the earnings of each department must be considered separately upon its own merits and rates must be determined for each department and be reasonable *per se*. The company cannot offset a deficiency in return from one business as against an excess in return from its other business, but each department must stand on its own foundation and bear its own burdens.⁵

In the light of all the facts and circumstances, the fixing of rates by the Board for the international air mail

⁵ *Re Syracuse Lighting Co.*, 30 P. U. R. (N. S.) 385.

operations of the carrier without offsetting the earnings from the carrier's domestic business was consonant with the principle that where a company is rendering two distinct types of service, each service should be treated separately for rate-making purposes. This basic principle of rate-making has never been foreign to the Board's thinking on the problem. The Board has frequently declared that, having once fixed final rates for one division of an air line, on the assumption that such division is a separate unit for rate-making purposes, this prior classification may not be retroactively invalidated by later inconsistently characterizing a second division of the same airline as a member of a joint or system rate-making unit.⁶ That the Board has no authority to retroactively revise a final rate is discussed in Part III. *infra*.

The Postmaster General contends that the Board's decision in the instant case departs from its prior consistent construction of the Act to the effect that the need referred to in Section 406(b) is that of the air carrier as a whole and not that of any particular geographical division of its operations. In support of this contention Petitioner has cited, at page 11 of his brief, six decisions of the Board rendered in 1942 and 1943. An examination of these cases discloses that the decisions related to carriers which were either wholly domestic or wholly international operations. None of the cases cited by Petitioner, including the *Pan American Mail Pay Case* in 1944,⁷ dealt with a carrier that had both domestic and international operations. None of these cases, therefore, are authority for the proposition that the Board is scrapping "a long standing and heretofore consistent construction of the Act."

Aside from the fact that none of the case cited by Petitioner support his contention that the need referred to in Section 406(b) is that of the air carrier as a whole and not that of any particular geographical division of its op-

⁶ *Pennsylvania Central Airlines Corporation, et al., Motions*, 8 CAB 685, 703 (1947).

⁷ *Pan American Airways, Alaska Mail Rates*, 6 CAB 61, 67.

eration, it must also be pointed out that in the cited cases the rates for the different routes or divisions were *open*. For example, in the *Pan American Mail Pay Case*, *supra*, the Board said that because of excessive earnings in the Latin American division, the Alaskan Division would be given compensatory mail pay only and would not be given sufficient mail pay to result in earnings on the investment properly allocated to the Alaskan division alone. However, in that case the rates for both the Latin American division and the Alaskan division were *open*, both divisions being on *temporary* rates and neither division was on a *permanent* rate. In the instant case, while the Latin American division rate was open, the domestic division rate was *closed* and had been closed since 1948. What the Board can or should do where the mail rate was temporary and open is entirely different from what the Board can or should do when the mail rate is closed and permanent.

The Board's decision in the instant case does not fly in the face of any specific directive in Section 406(b) but, on the contrary, was not only contemplated but authorized. The expert judgment of the Board, after considering all factors, things and conditions, should not be lightly set aside. Congress has delegated certain duties and responsibilities to the Board and requires it to exercise a rational judgment upon certain facts in order to ascertain public interest, convenience and necessity. As this Court aptly said in *American Airlines v. Civil Aeronautics Board*, 192 F. 2d 417, 420:

"It is in the exercise of that sort of judgment that the much discussed expertise of administrative agencies, finds its greatest value. Here is the field of uncertainties, imponderables and estimates. This is where the rule that a conclusion within the realm of rational deduction or inference stands despite difference of opinion, has its greatest applicability."

II.

TREATING THE CARRIER'S INTERNATIONAL DIVISION AS A SEPARATE RATE-MAKING UNIT WAS PROPER AND JUSTIFIED.

The Board committed no error in viewing C&S' Latin American operation as a separate carrier for rate-making purposes. As pointed out above, it not only possessed statutory authority, but also enjoyed administrative discretion to do so. We agree with the Board that as a practical matter it was desirable to treat the international division separately.

In the Board's "Statement of Tentative Findings and Conclusions" (J. A. 20) it acknowledged its responsibility to place carriers on final future rates as rapidly as possible. The task of placing a carrier with both domestic and international divisions on final future rates is an exacting one, and much more difficult than in the case where the carrier operates solely in the domestic or solely in the international field because many of the considerations which enter into the fixing of an international rate are different from those entering into the establishment of a domestic rate. Congress recognized the basic differences between domestic and international operations by providing in Section 801 of the Act that any certificate authorizing an air carrier to engage in "overseas or foreign transportation" shall be subject to the approval of the President. The President's approval is not required with respect to purely domestic operations. In other words, Congress, by requiring approval of the President before a certificate authorizing overseas transportation could be issued, gave formal recognition to the fact that a distinction existed between domestic and international air transportation. The basic reasons underlying the enactment of Section 801 of the Act are present and equally applicable *in fixing rates* for the transportation of mail on an international division, and fully justify the Board in

treating the international division as a separate rate-making unit and determining its need without offsetting past earnings of the carrier's domestic division.

The Court may well take judicial notice of the competition encountered by United States air lines in foreign transportation and particularly competition from air lines of foreign governments. These foreign air lines are not subject to the same degree of control and regulation in conducting air transportation to and from points in the United States as are the lines of the United States. Necessarily, therefore, the air lines of the United States engaged in foreign transportation and in competition with foreign air lines, must be given every advantage and opportunity to compete on the same level and under the same conditions with foreign air lines or else the efforts of the United States lines to engage in foreign transportation would be effectively thwarted. These are the reasons why the Board has maintained that "The vast extent of our future international air transportation operations and their economic and political significance is of great importance."⁸

In recent years a number of domestic carriers have entered the international field. These carriers are still in the early stages of development and experimentation. Energetic management and economic incentives are necessary if they are to meet the competition of foreign flag carriers. If, as contended by the Postmaster General, the domestic service of a United States carrier is to be burdened with the losses of its international service, the natural tendency would be to discontinue entirely or seriously curtail foreign service. Such a policy would deter other domestic carriers from even entering the foreign field. This fact was undoubtedly present in the mind of the Board when it concluded that the best interests of the United States would be served by not offsetting the earnings from C&S' domestic operation against "the 'need' resulting from the carrier's international routes."

⁸ *Northeast Air, et al., North Atlantic Routes*, 6 CAB 319, 325.

Aside from practical policy considerations designed to establish, encourage and promote foreign air transportation, it cannot be questioned that the Board's action in refusing to burden the domestic operation of C&S with its foreign operations is a proper and valid exercise of its general regulatory authority under the Act.

III.

THE BOARD HAS NO AUTHORITY TO OFFSET EARNINGS OF DOMESTIC DIVISION ARISING UNDER UNCHALLENGED FINAL RATES AGAINST THE NEED OF THE INTERNATIONAL DIVISION.

The Board, in its "Statement of Tentative Findings and Conclusions" (J. A. 21), based its decision not to offset any part of the earnings of the domestic division arising under unchallenged final rates against the need of the international division solely on reasons of economic policy. Although the Board, in its final opinion of October 18, 1951 (J. A. 55), specifically stated that it was not deciding the question of its legal power to make such an offset, we submit *that the Board had no statutory authority to make the offset* urged by the Postmaster General in the instant case.

The future rates established for the domestic division and applicable to the period beginning January 1, 1948, were *final* rates which were never challenged and are not now in issue. Since these permanent rates remained unchallenged,⁹ the Board is not empowered under the Act to retroactively revise such rates or to disturb past earnings arising thereunder by offsetting any part of the earnings earned under such rates.¹⁰ The offset of these earnings would, in effect, be a retroactive reduction of the final mail

⁹ On October 1, 1951 the Board (Order Serial No. E-5747) entered an order reopening the current final mail rates for the domestic operations of C&S and six other domestic trunk line carriers. On July 21, 1952 the Board (Order Serial No. E-6616) entered an order reopening the current final mail rate for the operations of C&S over its Latin American route.

¹⁰ *Transcontinental & Western Air, Inc. vs. CAB*, 169 F. 2d 893, 895, affirmed 336 U. S. 601 (1949), 93 L. Ed. 911.

rate for the domestic division. On this basis, the proposed offset would be plainly outside of the scope of the Board's jurisdiction as defined in the TWA case.¹¹

One of the most important of the statutory objectives, with which the Board is concerned, is to place carriers on permanent rates as rapidly as possible. The Postmaster General's reading of Section 406(b) would in effect preclude the Board from fixing a final rate for the domestic division of the carrier, would frustrate the statutory objective and would not harmonize with the clear purpose of the Act. Once having fixed a *final* rate for the domestic division alone, thereby segregating it as a rate-making entity, the Board cannot *retroactively* invalidate that rate by treating the domestic division as part of a new rate entity—the system—rather than an entity in and of itself.

If the Board had authority to make rates retroactive to any point of time, it would also have authority to offset past earnings as urged by the Postmaster General. But the Supreme Court has held in the TWA case¹² that the Board does not have the power to fix a new mail rate and to make it retroactive for a period in which a final rate previously fixed by the Board was in effect and unchallenged by the initiation of a mail rate proceeding. The Board and the Postmaster General have the power to institute a proceeding looking toward decrease of the rate for the domestic division when it passes the bounds of reasonableness. This the Postmaster General failed to do during 1948-1950, the period of higher earnings. If the Board had thought the domestic rate too high it should have reopened the domestic case, and if the Postmaster General felt the domestic rate too high, he should have requested the Board to reopen the case. The Board should not now be required to use indirect methods to accomplish that which it failed to do by direct and available legal means. Not having the power to make rates retroactive

¹¹ Idem.

¹² Idem.

to any point of time, it necessarily follows that the Board lacks the power at a future date to offset past domestic earnings under a final rate.

It is firmly established law that a public utility rate deals only with the future. It is not concerned with reimbursements of past losses nor with recapture of past profits. The first sentence of Sec. 406(a) simply empowers and directs the Board to fix rates. In no other public utility statute has such language been construed to contemplate a retroactive rate-making authority. There is nothing in the legislative history of the Civil Aeronautics Act of 1938 to indicate an intention or understanding that the Act contemplated a retroactive rate-making authority. The Board has held that under the Act in fixing a rate for the future it cannot capitalize past losses.¹³

It is well established that a regulated utility cannot be required to give up excess earnings from past operations.¹⁴ To subject to recapture earnings of air carriers in excess of a fair and reasonable rate would tend to sap management of those very incentives that are, in a private economy, essential if we would strive for efficiency. Sound administration of the Act not only requires no retroactive authority but can best be achieved without it. This conclusion is consistent with the Board's administration of the Act since its enactment in 1938.

The Board lacks the power to take such retroactive action unless Congress has plainly specified such power.¹⁵ The language of the Act does not suggest that Congress intended to break with the traditions of rate-making. There is no reference in the statute to an offset of past earnings or to a diminution of past profits. We think that if Congress intended to provide for the recapture of past

¹³ *Pennsylvania Central Airlines Corp., et al., Motions, supra.* See also *Galveston Elec. Co. v. Galveston*, 258 U. S. 388, 66 L. Ed. 678, and *Georgia Ry. v. R. R. Comm.*, 278 F. 242, aff. 262 U. S. 625, 67 L. Ed. 1144.

¹⁴ *Board of Commissioners vs. N. Y. Tel. Co.*, 271 U. S. 23, 70 L. Ed. 808. *Newton vs. Consolidated Gas Co.*, 258 U. S. 165, 66 L. Ed. 538.

¹⁵ *Neild vs. District of Columbia* (1940) 71 App. D. C. 306, 314, *et seq.*, 110 F. 2d 246, 254, *et seq.*

profits through the process of offset, it would have spelled out the terms of the proposal in clear and unmistakable terms and would not have employed the phrases "shall take into consideration", "among other factors", and "all other revenue" which, if interpreted as now urged by the Postmaster General, would have a disastrous effect on the objectives of the Act. In view of the finality of the domestic rates, which stood unchallenged for more than three years, the Board is without power to offset the higher earnings of C&S' domestic division against the need of its international division.

IV.

THE BOARD IS NOT REQUIRED, UNDER SECTION 406(b) OF THE ACT, TO OFFSET EARNINGS FROM DOMESTIC OPERATIONS AGAINST THE "NEED" RESULTING FROM INTERNATIONAL OPERATIONS IN ESTABLISHING RATES APPLICABLE TO INTERNATIONAL OPERATIONS.

Assuming, *arguendo*, that the Board is legally empowered to offset earnings of the domestic division gained under a final rate in establishing proper rates for the international division, such power is discretionary rather than mandatory. The Postmaster General, however, contends that the Act *requires* the Board, in fixing the fair and reasonable rate of compensation to offset "all other revenue" of the carrier in determining the carrier's need. On the other hand, the Board and the carrier contend that while the Board is required by Sec. 406(b) *to take into consideration* the need of the carrier for mail compensation, together with "all other revenue", it is *not required to reduce* the carrier's mail pay with any part of such other revenue if there are sound reasons for not doing so as a matter of economic policy.

The Petitioner argues in his brief (page 14) that a carrier is to receive only such mail pay as it "needs" and

that such "need" is to be determined by *offsetting* "all other revenue" of the carrier. While Petitioner admits that it is the duty of the Board to fix mail rates in an amount which will provide the carrier with funds necessary to carry out the national air transportation policy, he denies the right of the Board to exercise any discretion in determining how much or how little in the way of mail pay is necessary to carry out the national air transportation policy. He contends that the duty of the Board *to consider* "all other revenue" means that the Board has no choice other than *to offset* "all other revenue". He further contends that the term "all other revenue" leaves no discretionary power in the Board to disregard a portion of such other revenue even if such act is justified by economic policy considerations and is necessary to carry out the national air transportation policy. Finally, Petitioner contends that the *source* of the carrier's "all other revenue" is immaterial and that the Board has no power, discretionary or otherwise, to disregard any portion of such other revenue, although "such other revenue" may have come either from non-carrier property or from a different class of service, as contemplated by the Act, and even though the national air transportation policy would be served best by disregarding a portion of the carrier's other revenue as the Board, in the exercise of its conferred discretion, did in the instant case. The limited and restrictive interpretation of the Act urged by Petitioner is so untenable that it would defeat the very purpose and scheme of the Act. We think that anyone reading the whole of the statutory provisions relative to the Board's authority to fix rates, and the various rate-making elements to be considered in fixing and determining fair and reasonable rates of compensation must conclude that the Board's interpretation of the Act is in harmony with the obvious design of the Act as set forth in Section 2 and Section 406(b).

A. The Meaning and Scope of Section 406(b) of the Act.

Section 406(a) of the Act directs the Board to fix "fair and reasonable" rates of compensation for the transportation of mail by aircraft. Section 406(b) of the Act provides that in determining the rate *in each case* the Board "shall take into consideration, among other factors"—

(1) the condition that the carrier holds and operates under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service;

(2) the standards respecting the character and quality of service to be rendered; and

(3) the need of each carrier for compensation sufficient to insure the performance of mail service.

The statute further provides that, in addition to the need of the carrier for compensation to insure the performance of mail service, the Board "shall take into consideration" a fourth factor, i.e., the need of the carrier for compensation to enable it "to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service and the national defense".

Congress fully recognized that there were "other factors" besides those above enumerated which the Board should consider in determining the rate in each case. Some of these "other factors" are set forth in the first sentence of Section 406(b), and include (1) conditions peculiar to transportation by aircraft; (2) conditions peculiar to the particular air carrier; and (3) conditions peculiar to a class of air carriers.

In addition to those factors enumerated in Section 406(b) there are other factors which Congress expressly directed the Board to consider "as being in the public interest and

in accordance with the public convenience and necessity". These other factors are contained in Section 2 of the Act (Appendix).¹⁶

The Postmaster General admits in his brief, (page 8), that the factor of "need" is not the only factor to be considered by the Board, but contends that this single factor is mandatory in the sense that the Board cannot award mail pay in an amount in excess of what the carrier needs. In the first place, there is nothing in the Act which picks out the need factor from all the other factors above enumerated and says that this one factor is a mandatory limiting feature. It is no more mandatory or limiting than any of the other factors. It is only to be taken into consideration with all the other factors, and the weight to be given to it rests in the experienced judgment and broad discretion of the Board. In the second place, Congress, in Section 2 of the Act, only directed the Board to "consider" certain special factors, and in Section 406(b) only directed that the Board "shall take into consideration" certain other special factors. Both sections of the Act give leave to the Board to consider customary rate-making factors not mentioned in either section. In Section 2 Congress used the phrase "among other things" and in Section 406(b) Congress used the phrase "among other factors". Congress rightfully left to the Board the power to determine what other factors and things should be considered, as well as what weight should be given to each factor, in furthering the public interest, convenience and necessity. The Board must weigh all the criteria found in the Act which gives substance and vitality to Congressional mandate of policy set forth in Section 2 of the Act. These widely ranged factors were considered by the Board in this case.

¹⁶ In *American Airlines vs. Civil Aeronautics Board*, 192 F. 2nd, 417, 420 (1951) this Court said "Whatever belittling significance may be attached to the fact that those provisions (Section 2) were under a title 'Declaration of Policy', they are in the statute, are peremptory, and are as much an enactment by the Congress as is any other section of the statute."

The *carrier's* need was only one of many factors for the Board to consider, and that factor obviously was not a mandatory or limiting one. A statutory provision directing an administrative agency to *consider* a particular factor *among other things or factors* is certainly not the equivalent of an express command to adopt a uniform course of action. Congress never intended or contemplated that the Board would or could adopt a uniform course of action that would fit all carriers or classes of carriers or classes of service. This becomes apparent in view of the very first sentence of Section 406(b) which provides that the Board shall consider the conditions peculiar to the particular air carrier or class of air carrier. By giving the Board the authority to fix different rates for different air carriers or class of air carriers and different classes of service, Congress recognized the practical impossibility of prescribing or of directing the Board to adopt a uniform course of action.

The Postmaster General further argues that the intent of Congress reflected in Section 406(b) of the Act is that the carrier is to receive only such mail rate as it needs, and that such need is to be determined by offsetting *all* and not some part of its other revenue.¹⁷ This argument is patently absurd, in view of the Postmaster General's admission that the Board has the power administratively to fix rates separately for different operating divisions of a carrier, as the Board has done in the instant case with respect to the domestic and international divisions of C&S. If the Board is *required* to offset *all* of the carrier's other revenue in determining the need of the international division, it must, in the instant case, offset *all* of the revenue of the domestic division and not a part of such revenue. The Board's position that it is only required *to consider* all of the carrier's other revenue is both reasonable and logical.

¹⁷ Petitioner's Brief, page 14.

There is nothing in the Act to support the Postmaster General's view that the source of the carrier's "all other revenue" is immaterial and that "all other revenue" must be offset in determining a carrier's mail rate need. Such view would not only penalize the efficient carrier and put a premium on inefficiency, but would also lead to such an absurd result that few would be hardy enough to venture into the field of foreign air transportation. For example, assuming, *arguendo*, that the Ford Motor Company operated an international route with a mail pay need clearly established at \$5,000,000 a year, and the company earned \$10,000,000 a year in its automobile manufacturing and sales. Under the Postmaster General's theory the Board would be required to offset all of the revenues of the automobile division against the need of the airline operations and as a result the airline operations would only be entitled to compensatory mail pay. What incentive would there be for the company to engage in the airline operation? What incentive would there be in the instant case for C&S to engage in foreign air transportation or in developing an economically profitable sound and efficient domestic operation?

It is fairly apparent that the Postmaster General's construction of the "all other revenue" clause in Section 406(b) would inevitably defeat the statutory objectives of the Act as defined in Section 2.

The only requirement in the Act is that the Board *consider* all other revenue. This the Board has done. It has not ignored the carrier's earnings from its domestic division in determining the need of its international division. It fully considered the need of the carrier for mail compensation, together with "all other revenue", and after weighing all factors concluded that there were sound reasons for not reducing the carrier's mail rate with any part of such other revenue as a matter of economic policy (J. A. 54).

B. The Need Factor.

The Postmaster General contends that the Board's construction of the Act would give the carrier a subsidy in excess of its actual need. The problem, of course, is to determine what is the carrier's actual need. According to the Postmaster General the Board should fix the need rate at a level to provide the carrier with sufficient income to (1) meet its entire operating charges; (2) pay its taxes; and (3) earn a fair rate of return on its invested capital. In other words, the Board should be limited to maintaining the carrier as an efficient going concern, and any payments in excess of the minimum amount required to insure the bare performance of mail service is in excess of the carrier's actual need and therefore is not authorized by the statute. The question is whether the Board is empowered by Section 406(b) to fix need mail rates which provide an allowance for incentive, developmental and other purposes in excess of that necessary to sustain an existing operation.

The Board is clearly empowered to do so. Section 406(b) does not limit the fair and reasonable rate to the minimum amount necessary to maintain an existing operation, nor is the statutory concept of "need" so limited. On the contrary, the term "need" as employed in Section 406(b), expressly includes not only the mail rate necessary to "maintain" a given operation, but also the mail rate necessary to "continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service and the national defense". The extent of a carrier's need is the extent of mail rate actually required to accomplish these developmental objectives. The powers conferred in administering the mail pay provisions of the Act obviously were designed and intended to be coextensive with the over-all policy responsibilities placed upon the Board. Due regard for the developmental directions contained in the Act has been recognized by the Court to

be "peremptory" upon the Board in certificate cases,¹⁸ and should be recognized as being equally peremptory in mail rate cases.

The Board has always considered that it has statutory authority to allow a mail rate in excess of minimum operating need for incentive and developmental purposes. The entire purpose of "need" payments is not simply to make a carrier financially whole, but to develop an air transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service and of the national defense. The Board's decision not to reduce the carrier's international mail pay with any part of its domestic earnings was not based on whether offsetting the domestic profits would or would not deny C&S a fair rate of return on each of its divisions, but was based on sound reasons of economic policy. If the Board, in the administration of the Act, is to accomplish the stated objectives for which it alone was created, it must be concerned not only with the costs of operation and a fair return on capital, but also with establishing incentives to operate efficiently, with resulting benefits to the public and eventual self-sufficiency to the end that the financial aid given will bring about, at the earliest possible time, the kind of air transportation system contemplated by the Act. To accomplish this may require in a particular case, as here, the inclusion of compensation in the rate for incentive and developmental purposes. The meaning which the Postmaster General seeks to have fastened on the word "need" is to limit such need merely to provide the carrier with sufficient income to maintain it as a going concern. This, conceivably, could be done in the instant case by adopting the offset policy and using the profits from the carrier's domestic operation to sustain its international operation, but, by doing so, it would destroy the carrier's incentive to improve and develop its air transportation system. The basic underlying

¹⁸ *American Airlines vs. Civil Aeronautics Board, supra.*

question is simply—does the Act confer discretionary power on the Board to determine the need of this particular air carrier?

C. The Act Confers Discretionary Powers on the Board to Exclude "Other Revenue" Where Such Action Effectuates Statutory Policy.

One of the basic objectives of the Act is to foster and develop a greater degree of operating efficiency in the industry, with a view to ultimate self-sufficiency.¹⁹

The duty of developing the air transportation system rests upon the Board and not upon the Postmaster General, and the Board's judgment as to the need of the particular air carrier should be conclusive.

The Postmaster General contends that the Board lacks discretionary power to find that the earnings from C&S' domestic routes should not be used to offset the "need" resulting from the carrier's international routes, even though the Act does authorize the Board to fix rates separately for the different operating divisions of the carrier.

Section 406(b) of the Act clearly vests in the Board the duty to consider all possible and pertinent factors, including the factor of the carrier's need, and equally clearly vests in the Board the discretion to exclude "other revenue", if such action will best effectuate the statutory policy. The Board has, on many occasions, stated its position that the "all other revenue" clause of Section 406(b) affords it discretion with regard to the propriety of recognizing such items for the purpose of reducing "need" in final rate proceedings.

The provisions of Section 406(b) plainly indicate that the determination of "the need of each such carrier" involves the exercise of sound administrative judgment.²⁰ The basic purpose of the need clause of Section 406(b)

¹⁹ *Pennsylvania Central Airlines, et al., Motions*, 8 C. A. B. 685, 696-697 (1947).

²⁰ *Pan American Airways Co. (Del.), Transatlantic Mail Rates*, 1 CAB 220, 253 (1939); *American Airlines, Inc., Mail Rates*, 3 CAB 323, 336 (1942).

is to assist in the development of the air transportation system of the United States. Accordingly, it is self-evident that in cases where reduction of the "need" of the carrier's international division, by offset of earnings of the domestic division, would not in the judgment of the Board serve to foster and develop the air transportation system contemplated by the Act, the Board in its discretion may properly refuse to make such offset. Even if the Court disagreed with the Board on that proposition, the Board's decision would not necessarily be invalid because there would remain the exercise by the Board of the discretion plainly conferred upon it by Section 2 of the Act.

The Postmaster General's construction of the Act would leave no room for discretion and would require the Board to "offset" earnings of the domestic division in determining the rate for the international division in complete disregard of other special and traditional rate-making factors and the stated objectives of the Act. The word "offset" does not appear in Section 406(b) of the Act. The Postmaster General's construction that "offset" is required cannot reasonably be inferred from the express statutory language that the Board "shall take into consideration, among other factors," . . .

V.

THE BOARD'S INTERPRETATION OF SECTION 406(b) OF THE ACT IS REASONABLE AND PROPER.

The Board, in its "Statement of Tentative Findings and Conclusions" (J. A. 19), stated that it had considered the possible offset of a portion of the revenues realized by C&S under its domestic mail rate against the need which would otherwise be found to exist in relation to C&S' international operation, with a resulting reduction in the mail pay to be provided for such operation, but it found that policy considerations rendered such offset inappropriate in this case. In its final opinion (J. A. 54) the

Board reaffirmed its earlier view and concluded that, *as a matter of economic policy*, sound reasons existed for finding that the earnings from C&S' domestic routes should not be used to offset the "need" resulting from the carrier's international routes. The refusal of the Board to make the proposed offset was based on its interpretation of Section 406(b) together with the other provisions of the Act, particularly Section 2 thereof. The Board properly concluded that the offset policy proposed by the Postmaster General in the instant case was not in the public interest. The conclusion not to recapture past earnings over a substantial period of time was in line with established Board policy.

The Board on numerous occasions has determined that considerations of economic policy under the Act render it inconsistent with the public interest to affect retroactively rates for air mail compensation so as to require refund to the Government of moneys paid over an extensive period of time. To this effect, in *Pan-American Grace Airways, Mail Rates*,²¹ the Board held:

"Other considerations have been advanced against the adoption of a policy which would involve the recapture of past earnings accumulated over a substantial period of time. Without doubt, even under the most favorable circumstances, the policy would impede long-range planning and would inject a measure of uncertainty into undertakings looking toward the expansion and development contemplated by the Civil Aeronautics Act. It would in all likelihood reduce managerial incentive to accomplish increased economies in operation. Management could hardly be expected to exert itself energetically to such purpose with the ever-present fear, however unfounded it might be, that money saved through increased economies would be taken away. * * *"

Accordingly, the Pan American-Grace earnings held by the Board to be excessive were not recaptured. This same

²¹ 3 CAB 550, 564-565 (1942).

policy has been consistently maintained in a series of subsequent rate cases both domestic and international.²²

We have previously stated that one of the primary objectives of the Act is to further the development of the air transportation industry to a point where it will attain a self-sufficient status. Unquestionably, this goal is best obtainable by placing carriers on permanent rates rather than on a cost-plus basis for mail payments.²³ It is only under permanent rates that a carrier has the incentive to operate efficiently on the theory that it may retain any profits it earns in excess of the estimated return to be afforded by its mail rate.

In fixing the final domestic rate in the 1948 *C&S Domestic Mail Rate Case*,²⁴ the Board in commenting upon the estimated rate of 7.4% stated:

" * * any economies which the carrier's management succeeds in accomplishing through affective cost controls or improved operating procedures and techniques, which served to avert or mitigate anticipated increases in prices and to decrease operating costs below the unit cost of 116.6 cents per revenue plane mile estimated herein, will insure to the carrier in the form of higher earnings." (Emphasis Supplied).*

In other words, the Board specifically held that a 7.4% return was not to be considered a ceiling, and encouraged the carrier's management to increase the rate of return through progressive management policies.

The Postmaster General was a participant in the above proceeding but took no exception to the Board's findings and policy above quoted, although the C&S international division was on a temporary rate basis at the time. The Board's holding in the 1948 domestic case was no more nor less than an undertaking (joined in by the Postmaster

²² *Pan-American Airways, Inc., et al., Latin American Rate Case*, 3 CAB 657 (1942); *Eastern Air Lines, Inc. Mail Rate Proceeding*, 3 CAB 733 (1942); *American Air Lines, Inc. Mail Rate Proceeding*, 3 CAB 770 (1942).

²³ *Transcontinental & Western Air, Inc. vs. C. A. B.*, *supra*.

²⁴ 9 CAB 786, 812 (1948).

General through acquiescence) not to recapture domestic earnings in excess of 7.4%. The Postmaster General took no steps to review C&S' domestic rate as he could have done through appropriate legal action, and therefore as a matter of equity and fair play he should not now be heard on his contention that the higher domestic earnings should be recaptured in the international rate.

The adoption of a policy of offsetting profits of a domestic division *earned under a final rate* against the need of the carrier's international division would constitute a real deterrent to operating economy and efficiency. The Board has also recognized that, as a practical matter, if past domestic earnings are to be taken from a carrier to offset the need of its international division, there would be no incentive to live within the domestic rate. Instead of the carrier becoming self-sufficient over a period of time, as is the case under the Board's present policy, it would become increasingly more dependent upon a mail pay subsidy and never reach the goal of self-sufficiency.

The Board has frequently recognized its responsibility to place carriers under permanent rates. The Board's experience has shown that, as a practical matter, unless a permanent rate can be fixed for domestic operations without the necessity for determining simultaneously the rate for international division, it may often prove to be impossible to fix any permanent rate for any division for an extended period of time. We submit that adoption of the offset policy would deprive the Board of the power to fix *final* future rates on a divisional basis. In practical effect, any carrier with one or more divisions of its system operating on a temporary rate will be operating its entire system on temporary rates until such indefinite future time as rates have been finalized for each and all of the operating divisions.

If the offset policy were adopted, thus permitting the Board, in effect, to recapture past earnings on domestic operations under permanent mail rate order, serious

financial confusion would follow. Such a policy would not only impede long-range planning, but would inject great uncertainty in any plan of the carrier to expand and develop, as no large commitment would be conclusively feasible. Such a policy would reduce incentive instead of rewarding efficiency. Such a policy would mislead investors and would impair the carrier's ability to attract capital, because no financial statement could correctly reflect the carrier's financial status, no dividend declaration would be secure, and no offering of securities would have a firm foundation.²⁵

Under the procedure urged by the Postmaster General profits would be confiscated retroactively after stockholders have been assured of earnings, dividends have been declared and paid, new equipment has been purchased and all company economic and financial policies have been formulated on the justifiable assumption that such profits were real.²⁶

The Board, in refusing to adopt the offset policy in the instant case, recognized the likelihood that the domestic and more robust segment of the industry would be unfairly burdened with the economically weaker international segment. The Board correctly reasoned that such course would be contrary to the public interest, for if the domestic segment was kept strong and financially sound, fare reductions would follow, more modern aircraft would be acquired, and safer and more efficient operations would result. It is obvious that if the carrier's domestic division now, at long last on the road to self-sufficiency, is to be burdened with the comparatively infant and far from self-sufficient international operation, the efficient and economical carrier would either refuse to continue in, or refuse to enter into, the present financially unprofitable for-

²⁵ *T. W. A. v. CAB, supra.*

²⁶ The permanent domestic mail rate of C&S was established and set with no indication either in the Opinion and Order (Order Serial No. E-1825, Docket Nos. 1335 and 1897, adopted July 28, 1948) or in the rate case conferences with the Board's staff that any profits made thereunder would be subject to recapture in the international rate case.

eign or international service. The inevitable result would be that the international field would be dominated by air carriers operating under foreign flags and the foreign commerce requirements, the Postal Service and the national defense of this country would suffer, contrary to the purposes and design of the Act. It is submitted that these considerations are of extreme importance to the maintenance and development of both domestic and foreign air service, and that the two types of service must be kept separate and apart if either are to thrive and maintain a competitive position in their respective fields.

The Board's policy in not offsetting domestic profits is desirable from a purely administrative standpoint, because in administering the Act it is highly desirable to maintain a comparative status between domestic operators which have foreign routes, as against those which do not have foreign routes. Maintaining such comparative status has enabled the Board to fix uniform domestic mail rates for groups of carriers. This would not be feasible or possible if the Board lacked the power to exclude from consideration the needs of international operations. If the Board were required to fix rates for both domestic and international operations at the same time, it would be practically impossible to find a suitable basis for a comparison technique of analysis. The Board's long experience has shown that the comparison technique of rate-making is the most desirable to follow.

The adoption of a policy of offsetting profits of a domestic division while in a final rate against the need of the carrier's international division would unfairly penalize the carrier especially in view of the fact that had domestic losses been suffered during this period they could not have been recovered by the carrier through its final international mail rate. While operating under a final rate, the carrier takes the risk of loss, without possibility of later reimbursement through mail pay and it is therefore only equitable that the carrier should retain the benefit of good earnings resulting from keen management.

In view of the foregoing arguments, we submit that the Board's interpretation of Section 406(b) of the Act is both reasonable and proper.

VI.

THE BOARD'S INTERPRETATION OF SECTION 406 (b), BEING PROPER AND REASONABLE, SHOULD BE BINDING UPON THE COURT ON A PETITION FOR REVIEW.

Since the parties have stipulated that no facts are in controversy, the primary question before this Court is one of law and is whether the Board's interpretation of Section 406(b) of the Act should be sustained.

The Board, in its well considered opinion of October 18, 1951, concluded that in fixing just and reasonable air mail rates for the Latin American routes of C&S, it was not required under Section 406(b) of the Act to offset past earnings from the carrier's domestic operations and decided "for reasons of economic policy" that the rates to be prescribed for the carrier's international routes should not be reduced by any amount of the earnings from its domestic operations. As has been previously discussed, there is warrant in the record and a reasonable basis in law for the Board's interpretation of the statute.

It is a well settled principle, supported by numerous decisions, that the Court should give great weight to the construction placed upon a statute by an administrative agency charged with the responsibility for the administration and enforcement of the statute. In *Brooks Transp. Co. v. United States*, 93 F. Supp. 517, affirmed 340 U. S. 325, 95 L. ed. 668, the Court said, "Though the question here involved is one of law, it is well settled that the courts should give great weight to the Commission's interpretation of the Act." As Mr. Justice Burton stated in his opinion in *Levinson v. Spector Motor Co.*, 330 U. S. 649, 672, 91 L. ed. 1158, "in the light of the Commission's long

record of practical experience with this subject and its responsibility for the administration and enforcement of this law, the conclusions (of the Commission) are entitled to special consideration." See also *United States v. American Trucking Associations*, 310 U. S. 534, 549, 84 L. ed. 1345; *Colgate Palmolive Peet Co. v. United States*, 320 U. S. 422, 426, 88 L. ed. 143; *McLean Trucking Co. v. United States*, 321 U. S. 67, 87-89, 88 L. ed. 544.

The national air transportation policy, as provided for under Section 2 of the Act, expressly requires the Board to consider, among other things, the encouragement and development of an air transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States; the regulation of air transportation in such a manner as to recognize and preserve the inherent advantages of, and foster sound economic conditions in, such transportation; the formation of adequate, economical, and efficient service by air carriers at reasonable charges; competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense; the regulation of air commerce in such manner as to best promote its development and safety; and the encouragement and development of civil aeronautics. Resolving these considerations, in determining whether air mail rates for international routes will effectuate the overall air transportation policy, is a complex task which requires extensive facilities, expert judgment and considerable knowledge of this form of transportation. Congress has left this task to the Civil Aeronautics Board. The experience and the wisdom of the Board, not of the Court, or of the Postmaster General, must determine the question of reasonable and proper rates. As Mr. Justice Rutledge said in *McLean Trucking Company v. United States*, 321 U. S. 67, 88, 88 L. ed. 544, 557, "If the Commission did not exceed the statutory limits within

which Congress confined its discretion and its findings are adequate and supported by evidence, it is not our function to upset its order."

In attaining the objectives of the national air transportation policy, it is the function of the Board to interpret the language used by Congress to carry out the legislative intent. The Board is trained for this purpose. Administrative interpretation of a statute carries persuasiveness as an expression of view of those experienced in the administration of the Act and acting with the advice of a staff specializing in its interpretation and application. *Overnight Motor Transp. Co. v. Missel*, 316 U. S. 572, 86 L. ed. 1682. Administrative agencies designated by Congress as specialists in a particular field and advised by experts are in a better position than a reviewing Court to determine appropriate applications of statutes which they are directed to administer. *National Labor Relations Board v. Medo Photo Supply Corporation*, 135 F. 2d 279, affirmed 321 U. S. 678, 88 L. ed. 1007.

To sustain the Board's interpretation of Section 406(b) the Court need not find that the Board's construction is the only reasonable one, or even that it is the result the Court would have reached had the question arisen in the first instance in judicial proceedings. The reviewing Court's function is limited. All that is needed to support the Board's interpretation is that it has a warrant in the record and a reasonable basis in law. *Unemployment Compensation Commission v. Aragon*, 329 U. S. 143, 153, 154, 91 L. ed. 136, 145, citing *National Labor Relations Board v. Hearst Publications*, 322 U. S. 111, 88 L. ed. 1170, and *Rochester Telephone Corp. v. United States*, 307 U. S. 125, 83 L. ed. 1147.

In *American Airlines v. Civil Aeronautics Board*, (7th Cir. 1949), 178 F. 2d 903, the petitioners sought to review an order of the Board authorizing air freight forwarders to engage indirectly in interstate air transportation. Petitioners contended that the Board's findings were insufficient

to sustain the order and that the Board erroneously interpreted the law. The Court found that there were sufficient findings upon which the Board based its order and sustained the interpretation the Board gave to Section 408(b) of the Act. The Court stated:

"Obviously, we are not concerned with the question of whether this was a wise course of action. Nor are we concerned with whether we would have entered the order ourselves or whether the board's interpretation is the only reasonable one. Our function is limited; we may only inquire as to whether the board's interpretation of the statute has warrant in the record and a reasonable basis in the law. *Unemployment Compensation Commission v. Aragon*, 329 U. S. 143, 153-154, 67 S. Ct. 245, 91 L. ed. 136. See also *National Labor Relations Board v. Hearst Publications*, 322 U. S. 111, 131, 64 S. Ct. 851, 88 L. ed. 1170.

"It would seem unnecessary to reiterate that presumptively the board's order is correct, and, under any and all circumstances, its decision is entitled to great weight. It is not for the federal courts to supplant the Commission's judgment even in the face of convincing proof that a different result would have been better."

In concluding, the Court said:

"We think that the interpretation of the statute by the board in order to avoid incongruous result and in order to effectuate the intent of Congress was proper under *United States v. American Trucking Ass'ns*, 310 U. S. 534, at 542-544, 60 S. Ct. 1059, 84 L. ed. 1345 and authorities there cited. To the same effect is the recent decision of the Court of Appeals for the Second Circuit in *North American Utility Securities Corp. v. Posen, et al.*, 1949, 176 F. 2d 194. We conclude that the board's interpretation of the second provision of Section 408(b), which makes it inapplicable to the acquisition of control of an air freight forwarder, carries out the intent of Congress and is a reasonable and proper interpretation of that provision binding upon this court. *National Labor Relations Board v. Hearst Publications*, 322 U. S. 111, 130, 64 S. Ct. 851, 88 L. ed. 1170; *Unemployment Compensation Commission v. Aragon*, 329 U. S. 143, 153-154, 67 S. Ct. 245, 91 L. ed. 136."

In the case of *United States v. American Trucking Association*, 310 U. S. 534, 549, 84 L. ed. 1345, the question raised on review was as to the meaning of Section 240(a) of the Motor Carrier Act of 1935. The Supreme Court upheld the construction given to the statute by the Interstate Commerce Commission and stated that administrative interpretations of a statute are entitled to great weight where they involve a contemporaneous construction of the statute by the persons charged with the responsibility of setting its machinery in motion and of making its parts work efficiently and smoothly.

In *National Labor Relations Board v. Denver Bldg. & Const. Council*, 341 U. S. 675, 95 L. ed. 1284, the Supreme Court upheld an order of the National Labor Relations Board and reversed a judgment of the United States Court of Appeals for the District of Columbia refusing to enforce the Board's order which enjoined a labor organization from engaging in a strike. The Court accepted the holding of the Board that the strike was an unfair labor practice within the meaning of section 8(b)(4)(A) of the National Labor Relations Act. The Court stated:

"Not only are the findings of the Board conclusive with respect to questions of fact in this field when supported by substantial evidence on the record as a whole, but the Board's interpretation of the Act and the Board's application of it in doubtful situations are entitled to weight."

Among numerous other decisions which have held that Courts must give great weight to an administrative agency's interpretation of its governing statute are *West Texas Utilities Co. v. NLRB*, 184 F. 2d 233, 87 U. S. App. D. C. 179, certiorari denied 341 U. S. 939, 95 L. ed. 1366; *Billings v. Truesdell*, 321 U. S. 542, 88 L. ed. 917; *Augustus v. Commissioner of Internal Revenue*, 118 F. 2d 38, certiorari denied 313 U. S. 585, 85 L. ed. 1540; *Bowles v. Mannie & Co.*, 155 F. 2d 129, certiorari denied 329 U. S. 736, 91 L. ed. 636; *Railroad Retirement Board v. Duquesne Warehouse Co.*,

149 F. 2d 507, 80 U. S. App. D. C. 119, affirmed 326 U. S. 446, 90 L. ed. 192.

In its "Statement of Tentative Findings and Conclusions" adopted May 18, 1951, and in its decision of October 18, 1951, the Board applied the principle that while it is required to take into consideration the need of a carrier for mail compensation, together with "all other revenue," it is not required by Section 406(b) to reduce the carrier's mail pay with any part of such other revenue if there are sound reasons for not doing so as a matter of economic policy (J. A. 54). We see nothing in the Board's view to require the Court to substitute a different construction of Section 406(b) from that made by the Board which is entrusted with the responsibility of administering it and the duty of effectuating the declared policy and purposes of the Act.

The construction urged by the Board of Section 406(b) is consistent with the language of that section and with the policy of the Civil Aeronautics Act with respect to the encouragement, development and regulation of air transportation required for the commerce of the United States, the Postal Service and the national defense. The Postmaster General's construction runs counter to the declared policy of the Act and in view of the express language of Section 406(b), is unwarranted.

The Board, not the Postmaster General, is charged with the administration of the Act for the purposes and policies declared in the Act. The Board, a skilled and experienced body, is entrusted with the responsibility of initially applying the statutory provisions to the facts of each particular case. Its interpretation that it was not required under Section 406(b) of the Act to offset excess past earnings of the carrier in its domestic operations in fixing mail rate for the carrier's Latin American operations is supported by the record and has a reasonable basis in law. As a matter of law, the Board's interpretation should be accepted by this Court and the Board's decision of October 18, 1951 should be sustained.

CONCLUSION.

The regulatory function of the Board, insofar as it includes authority to fix rates for transportation of air mail, is a forward looking function. In that respect it differs from a purely judicial determination of present or past rights. When a regulatory action contemplates a new mail rate a type of judgment is required which is wholly absent from the mere valuation of past facts. In fixing and determining fair and reasonable rates of compensation under Section 406 of the Act, the Board must resolve the issue of public interest, convenience and necessity, not only upon the basis of insuring the performance of mail transportation service, but by also taking into account and giving appropriate weight to broad considerations of future welfare related to the development of the air transportation industry. The Board has well said that such an approach "must necessarily be predicated upon future estimates as well as present facts, for it is keyed to future goals and an effort to envisage the shape of things to come".

The Board, in fixing air mail rates for the Latin American operations of C & S, under its order of October 18, 1951, based its judgment on available facts as to present operations, business practices and past experience with air transportation operations. It also took into account and gave appropriate weight to the future welfare of the carrier and the development, encouragement and promotion of air transportation in accordance with the declared policy of the Act. In prescribing the rates which it considered to be consistent with the public interest, the Board did not exceed the statutory limits within which Congress confined its discretion. Its findings are supported by the evidence and comply with the requirements of the Act.

In the light of the Board's practical experience with air transportation, the Court should follow the interpretation of the statute given by the Board, the agency to which Congress has given the duty and imposed the obligation of administering the Act.

Upon the basis of the foregoing reasons and authorities,
the Board's order of October 18, 1951 should be affirmed.

Respectfully submitted,

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Dated: September 26, 1952.

APPENDIX.

The Civil Aeronautics Act of 1938, 52 Stat. 977, as amended, 49 U. S. C. 401, *et seq.*, provides in pertinent part as follows:

"DECLARATION OF POLICY

"Sec. 2. In the exercise and performance of its powers and duties under this Act, the Authority shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity—

(a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service and of the national defense;

(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by air carriers;

(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

(d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(e) The regulation of air commerce in such manner as to best promote its development and safety; and

(f) The encouragement and development of civil aeronautics." (49 U. S. C. 402)

"RATES FOR TRANSPORTATION OF MAIL

AUTHORITY TO FIX RATES

"SEC. 406. (a) The [Board] * * * is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, * * * and the

rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft." [49 U. S. C. 486(a).]

"RATE-MAKING ELEMENTS

"SEC. 406. (b) In fixing and determining fair and reasonable rates of compensation under this section, the [Board] * * *, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the [Board] * * * shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense." [49 U. S. C. 486(b).]

"THE PRESIDENT OF THE UNITED STATES

"Sec. 801. The issuance, denial, transfer, amendment, cancellation, suspension, or revocation of, and the terms, conditions, and limitations contained in, any certificate authorizing an air carrier to engage in overseas or foreign air transportation, or air transportation between places in the same Territory or possession, or any permit issuable to any foreign air carrier under section 402, shall be subject to the approval of the President. Copies of all applications in respect of such certificates and permits shall be transmitted to the President by the Authority before hearing thereon, and all decisions thereon by the Authority shall be submitted to the President before publication thereof." (49 U. S. C. 601).

JOINT APPENDIX

In the United States Court of Appeals
for the District of Columbia Circuit

No. 11,351

JESSE M. DONALDSON, Postmaster General of the
United States, and THE UNITED STATES OF
AMERICA on behalf of the Postmaster General
Petitioners,

v.

CIVIL AERONAUTICS BOARD, *Respondent*

Petition for Review of Order of the Civil Aeronautics Board

*United States Court of Appeals
For the
District of Columbia Circuit*

FILED JUL 10 1952

Joseph W. Stewart
CLERK

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**In the United States Court of Appeals
for the District of Columbia Circuit**

No. 11,351

JESSE M. DONALDSON, Postmaster General of the
United States, and THE UNITED STATES OF
AMERICA on behalf of the Postmaster General,
Petitioners,

v.

CIVIL AERONAUTICS BOARD, *Respondent*

Petition for Review of Order of the Civil Aeronautics Board

JOINT APPENDIX

IN THE UNITED STATES COURT OF APPEALS
FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 11,351

JESSE M. DONALDSON, Postmaster General of the
United States,

and

THE UNITED STATES OF AMERICA, On Behalf of the
Postmaster General, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

Petition for Judicial Review

*To the Honorable, the Judges of the United States Court of
Appeals for the District of Columbia Circuit:*

JESSE M. DONALDSON, Postmaster General of the United States, and THE UNITED STATES OF AMERICA, on Behalf of the Postmaster General, petitioners, respectfully present this petition for judicial review of orders of respondent, Civil Aeronautics Board, and in support thereof represent and allege the following:

I

**THE FACTS AND THE STATUTE UPON WHICH JURISDICTION
IS BASED**

1. This petition is filed pursuant to Section 1006 of the Civil Aeronautics Act of 1938, 52 Stat. 1024, 49 U.S.C. 646. It seeks review of orders of the Civil Aeronautics Board entered in proceedings under Section 406 of the Act, 49 U.S.C. 486, fixing mail pay for Chicago and Southern Air Lines, Inc. (Docket No. 2564, Orders No. E-5793 and E-6045, dated October 18, 1951, and January 18, 1952, respectively). This petition is filed within 60 days after entry of the Board's order of January 18, 1952, denying the Postmaster General's petition for reconsideration. Section 1006; *Braniff Airways v. Civil Aeronautics Board* (1945), 79 U.S. App. D. C. 341, 147 F. 2d 152.

2. The Postmaster General has a substantial interest in the air mail pay orders sought to be reviewed within the meaning of Section 1006 of the Act. He is a statutory party to all airmail pay proceedings before the Board, Sections 406(a) and 406(c), and as such serves as the protector of the public interest in such proceedings. *Seaboard & Western Air Lines v. Civil Aeronautics Board* (1949), 86 U. S. App. 64, 181 F. 2d 515, 518-519, certiorari denied (1950) 339 U. S. 963. The Postmaster General is required to pay air carriers for transporting air mail, out of funds appropriated by Congress for that purpose, at the rates fixed by the Board. Section 406(a). The Postmaster General participated in the proceedings before the Board in which the orders sought to be reviewed were entered, and there urged the objections raised in this petition.

II

THE NATURE OF THE PROCEEDINGS AS TO WHICH REVIEW IS SOUGHT

1. Chicago and Southern Air Lines, Inc. (C. & S.) is a certificated air carrier conducting both domestic and Latin-American operations. Service over the Latin-American routes was inaugurated November 1, 1946. Temporary airmail pay rates for these foreign operations were fixed by the Board by orders dated March 20, 1947 (7 C.A.B. 985) and May 6, 1948 (9 C.A.B. 924).

2. In July 1948, the Board fixed a final subsidy mail pay rate for C. & S.'s domestic operations effective January 1, 1946. 9 C.A.B. 786. The Board estimated that this rate would yield C. & S. a 7.4% return on its investment allocable to domestic operations. Actual operations under this rate, however, have resulted in an average annual return of 12.51% on domestic operations for the years 1948 to 1950. This is \$654,000 more than a 7.4% rate of return would have provided.¹

¹ On October 1, 1951, the Board reopened the current final mail pay rates for the domestic operations of C. & S. and six other domestic trunkline carriers. Order Serial No. E-5747.

3. On May 18, 1951, the Board issued a show cause order proposing final subsidy rates for C. & S.'s Latin-American operations. These proposed rates were retroactive for the period November 1, 1946, to December 15, 1950, and prospective from December 16, 1950. The Postmaster General filed objections to the proposed rates as excessive. He contended, *inter alia*, that the Board was required to offset the carrier's "excess" earnings on its domestic operations in determining the carrier's subsidy "need" on its foreign routes.

The Board, rejecting this contention, issued its opinion and order on October 18, 1951, fixing final mail pay rates, both retroactive and prospective, for C. & S.'s Latin-American operations.² The Board held that Section 406(b) of the Act did not require it "to reduce the carrier's mail pay with any part of [the carrier's] other revenue if there are sound reasons for not doing so as a matter of economic policy."³ The Board, in fixing the rate, determined that the carrier was entitled to a return of 7% for the past period and 10% for the future.

4. The Postmaster General filed a petition for reconsideration, which the Board denied on January 18, 1952. The administrative remedies of the Postmaster General before the Board have now been exhausted.

III

POINTS ON WHICH PETITIONERS INTEND TO RELY

1. Section 406(b) of the Act compels the Board to offset as "other revenue" the excess earnings of the carrier's domestic operations in determining its "need" for subsidy compensation when fixing mail rates for its international operations. The Board is not empowered to refuse

² The opinion and order were based upon a stipulation of facts entered into by the parties to the Latin-American mail pay proceeding.

³ This principle had been enunciated by the Board four months previously in *Western Air Lines, Inc.—Inland Air Lines, Inc., Mail Rates Case*, Order Serial No. E-5467, June 26, 1951. Petitioners are challenging in this Court the validity of that aspect of the Board's order in the *Western* case. *Donaldson, et al. v. Civil Aeronautics Board*, Docket No. 11,259, petition for review filed December 10, 1951.

to offset such excess earnings for reasons of economic policy or otherwise.

2. By failing to offset the excess earnings from the carrier's domestic operations in fixing rates for its international operations, the Board has fixed a rate which produces compensation in excess of the carrier's "need" as provided in the Act, and has allowed the carrier a rate of return in excess of the rate of return previously found reasonable by the Board.

3. The Board exceeded its statutory power or, in the alternative, abused its discretion in failing to offset C. & S.'s "excess" domestic earnings in fixing airmail pay rates on the carrier's Latin-American routes.

IV

THE RELIEF PRAYED

WHEREFORE, petitioners pray that the Board's order be modified to reduce the payments to C. & S. for the transportation of mail on its Latin-American routes by the amount that such payments fail to reflect the carrier's "excess" earnings on its domestic routes, and for such further relief as the Court may deem proper.

(Signed) H. G. Morison
H. G. MORISON
Assistant Attorney General
Department of Justice
Washington 25, D. C.

(Signed) Roy C. Frank
ROY C. FRANK
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(Signed) Frederick E. Batrus
 FREDERICK E. BATRUS
Assistant Solicitor

(Signed) Eugene J. Brahm
 EUGENE J. BRAHM
Chief, Air Mail Section
 Office of the Solicitor

Dated March 18, 1952

* * * * *

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E-5385

UNITED STATES OF AMERICA
 CIVIL AERONAUTICS BOARD
 WASHINGTON, D. C.

Served May 18 1951

Docket No. 2564

CHICAGO AND SOUTHERN AIR LINES, INC.
 Latin American Operations

In the matter of the compensation for the transportation of
 mail by aircraft, the facilities used and useful
 therefor, and the services connected
 therewith.

Adopted: May 18, 1951

Statement of Tentative Findings and Conclusions¹

BY THE BOARD:

This proceeding was instituted by petition filed October 11, 1946, by Chicago and Southern Air Lines, Inc., hereinafter referred to as C & S, for an order fixing and deter-

¹ This statement does not necessarily represent the view of all members with respect to all issues.

mining the fair and reasonable rates of compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, over its Latin American Route.

Informal mail rate conferences² have been held with C&S in order to evaluate past operating results, claimed mail pay and estimates for a future period as submitted by the carrier.

116 In accordance with Section 302.13 of the Procedural Regulations the Board has arrived at the tentative findings and conclusions and has formulated the tentative mail rates set forth herein. Concurrently, the Board is issuing an order directing C&S to show cause why such tentative mail rates should not be established as the final rates in this proceeding.

CERTIFICATE HISTORY

This route was awarded to C&S by the decision of the Board in the *Latin American Case* on May 17, 1946, approved by the President May 22, 1946.³ The route authorized operations between the co-terminal points, Houston and New Orleans, and Havana; from Havana one leg branched to San Juan by way of Camaguey, Port au Prince and Ciudad Trujillo; a second leg extended from Havana to Caracas by way of Kingston, Aruba and Curacao. In January 1947, service to Montego Bay, Jamaica, as an intermediate point between Havana and Kingston was authorized⁴ and in the *Latin American Route Amendment Case*⁵ in March 1949, Camaguey was eliminated and Kingston instead of Havana was made the branching point of the San Juan and Caracas legs.

² Pursuant to Rule 19 of the Board's Procedural Regulations. These conferences were held on January 10-12, 17-19, and 24-26, 1951.

³ *Latin American Air Service*, 6 CAB 857, 927 (1946).

⁴ *Service to Montego Bay*, 7 CAB 741, 747 (1947).

⁵ *Pan American Airways, et al., Latin American Route Amendment* 10 CAB 351, 380 (1949).

The initial petition of C & S filed on October 11, 1946 requested mail pay at the rate of \$1.73 per airplane mile. A subsequent amendment requested that this be increased to \$2.17. A temporary rate of 95 cents per airplane mile was set on March 20, 1947⁶ for the New Orleans-Havana segment.

On March 30, 1948, C & S filed a new petition requesting a rate of \$1.28 per airplane mile for performing the service between Houston-New Orleans and Caracas via Havana and Kingston, and on May 6, 1948 the Board authorized mail pay at the rate of \$1.25 for this service.⁷ This latter rate has been continued until the present time.

PERIODS FOR WHICH RATES WILL BE FIXED

Service from New Orleans to Havana was inaugurated on November 1, 1946. Service from Houston to Caracas via Havana and Kingston began August 1, 1948. The carrier has never begun operations to Aruba, Curacao and Montego Bay nor from Kingston to San Juan.

Service was begun with 50-passenger DC-4's. Constellation aircraft were introduced on December 16, 1950. This four-engine service was supplemented by DC-3 operations between New Orleans and Houston during the first six months of 1949. DC-3's have been in constant use on this segment since June 1950.

The past period for which mail rates will be fixed will be that from November 1, 1946 through December 15, 118 1950, the time during which the carrier was serving most of its system with DC-4 aircraft. The future period will begin December 16, 1950, the date on which service from New Orleans south was offered with Constellation aircraft.

⁶ Chicago and Southern Air Lines, Inc., Latin American Mail Rates, 7 CAB 985 (1947).

⁷ Chicago and Southern Air Lines, Inc., Latin American Mail Rates, 9 CAB 924 (1948).

MAIL RATES FOR THE PAST PERIOD

Scheduled Service Required

The various changes effected by C&S in the pattern of its service over its international system indicate a proper concern on the part of the carrier to develop to the utmost the traffic potentialities existing on its route. The carrier's experimental efforts in this direction, at least up through June 1949, were rewarded with a continually increasing system passenger load factor. The following table sets forth the quarterly available seat-miles, passenger-miles and load factor attained by the carrier on its international system.

CHICAGO AND SOUTHERN'S INTERNATIONAL SYSTEM
QUARTERLY TRAFFIC DATA UP TO JUNE 30, 1949

Quarter Ended	Revenue Passenger Miles (000)	Standard Available Seat-Miles* (000)	Revenue Passenger Load Factor (%)
March 31, 1947	1,773	4,819	36.79
June 30, 1947	1,297	5,244	24.73
Sept. 30, 1947	1,881	5,365	35.06
Dec. 31, 1947	1,747	5,305	32.93
March 31, 1948	1,993	5,365	37.15
June 30, 1948	1,927	5,455	35.33
Sept. 30, 1948**	4,158	10,680	38.93
Dec. 31, 1948	5,118	13,957	36.67
March 31, 1949	6,117	15,087	40.54
June 30, 1949	6,954	16,276	42.73

* DC-3 @ 21 available seats; DC-4 @ 44 seats.

** Service to Caracas inaugurated August 1, 1948.

119 During this period, as indicated, the carrier's load factors steadily improved concurrently with an increase in volume of service operated.

This period of load factor improvement accompanying an increase in capacity not only indicates the success of the carrier's experiments with different types of schedule patterns, but also justified in part at least the carrier's further experimentation with its schedules. Unfortunately, after June of 1949, such experimentation did not meet with

an equal degree of success. The following table indicates that continued schedule changes by the carrier resulted in the operation of substantial amounts of excessive capacity, with a corresponding drop in load factor.

CHICAGO & SOUTHERN INTERNATIONAL SYSTEM
QUARTERLY TRAFFIC DATA 1949 AND 1950

Quarter Ended	Revenue Passenger Miles (000)	Standard Available Seat-Miles* (000)	Revenue Passenger Load Factor (%)
3/31/49	6,117	15,087	40.54
6/30/49	6,954	16,276	42.73
9/30/49	7,832	24,220	32.34
12/31/49	6,424	24,109	26.65
3/31/50	7,100	23,514	30.19
6/30/50	6,882	21,294	32.32
9/30/50	7,362	17,773	41.42

* DC-3 @ 21 available seats; DC-4 @ 44 seats.

The drop in revenue passenger load factor which occurred in the third quarter of 1949 followed a substantial schedule change effected by the carrier on June 27, 1949, when three weekly round trips were added between Houston and Caracas via New Orleans and Kingston. The resulting pattern of service represented a substantially greater volume of revenue plane miles or available seat miles than that offered by C & S at any time to that date. The carrier claims that this increase in service volume was justified on the grounds that its load factor was steadily increasing up until the end of June 1949, that competitive services of other airlines, both foreign and United States Flag carriers, to and from Caracas were improving steadily during this period and that it had no foreknowledge that Venezuelan air traffic volumes would decline markedly from the end of June 1949 forward.

An examination of the facts indicates that while there is some merit to the carrier's position, no real justification has been established for the 75% increase in capacity scheduled to and from Caracas after June 1949. Although load factors between Kingston and Caracas had increased some eight percentage points from the first to the second

quarter of 1949, the load factor for the latter quarter was only 39.8%, a level which hardly justified a substantial increase in the volume of service rendered. While it appears that competitive services existed for Caracas traffic, it has not been shown that such competition was greatly intensified during the summer of 1949; and C&S's increasing load factor on the Kingston-Caracas segment prior to June 1949 would seem to have augured well for its continuing to obtain a reasonable share of the Caracas traffic. It should be noted, finally, that the carrier is restricted from transporting local traffic between Caracas and Havana by the Venezuelan government except on three weekly round trips, a fact which it knew would limit its loads on the added frequencies.

We have stated in other mail rate cases⁸ our concern over the tendency, on the part of some of the carriers, to add schedules on part or all of their systems without having a reasonable expectation that such greater service volumes would result in added revenue greater than 121 added expenses. Such a policy on the part of the carriers can only result in increases in break-even need and need for mail pay support. Similar results are inevitable where, as here, a carrier adds substantial service volume and fails to reduce it after seeing that the anticipated changes in the balance of revenues and expenses have not materialized. Since we do not propose to underwrite such excessive volumes of service with mail pay, nor to encourage management philosophy underlying such operation, we are impelled to disallow for mail rate purposes a substantial amount of the mileage operated by C&S during the past period.

As already noted, the service operated by the carrier was clearly excessive beginning in the third quarter of 1949. Relatively low load factors continued during the next three quarters, but this condition was rectified on May 29, 1950, when the carrier substantially reduced its service volume.⁹

⁸ Capital Airlines, Inc., Mail Rates, 10 C.A.B. 705, 710 (1949).

⁹ The schedule pattern beginning May 29, 1950, totalled 32,494 miles per week, a reduction of 20% from that operated in the average week during the preceding year.

It is therefore during the approximate 11-month period ended May 29, 1950, that the capacity disallowance will be made.

We do not propose to disallow during this period all of the mileage which now, in retrospect, might be termed excessive. To do so, would, in our judgment, be tantamount to charging C&S management with possession of the gift of infallible prophecy, a responsibility which we do not read into the standard of economic and efficient management laid down in Section 406(b) of the Civil Aeronautics Act of 1938, as being required of the carriers in operations to be underwritten with mail pay.

In determining the specific amount of the disallowance, therefore, we propose to recognize a reasonable period during which the mileage operated will be recognized for mail pay purposes. The purpose of such recognition 122 during this period is to allow C & S an experimental period, during which to test its higher service volume. The most productive schedule pattern operated by the carrier up to June 1950 in terms of load factor and load factor trend was that in effect from December 19, 1948 to June 27, 1949 consisting of approximately one and one-half weekly round trips between Houston and Havana, two and one-half between Houston and New Orleans, nine and one-half between New Orleans and Havana and giving service to Kingston and Caracas of four round trips per week. We find that the mileage operated by the carrier in excess of this schedule pattern during the year following June 1949 could be deemed excessive from the standpoint of load factors, traffic and revenues realized; but that in order to allow for a reasonable period of experimentation, only one-half of such excess will be disallowed for rate-making purposes. In effect, this finding recognizes a period of approximately five and one-half months of the mileage as actually operated, since such operation continued for a total of approximately eleven months.

In view of the fact that on May 29, 1950 the carrier evolved a schedule pattern which reduced by some 20 percent the plane miles operated in the average month during

the preceding year we find that the schedule pattern operated from May 29, 1950 through December 15, 1950 should be recognized in its entirety for mail rate purposes.

The effect of this determination is to disallow 341,000 plane miles operated by C & S up through May 28, 1950 and to recognize the plane mileage operated from that date through December 15, 1950. Appendix No. 1 compares the plane miles, standard available seat-miles, and standard available ton-miles actually operated by the carrier up through December 15, 1950 and that which has been recognized consistent with the above determination.

123 As shown in Appendix No. 1, the 341,000 miles disallowed in the past period approximates 12 percent of that operated by the carrier during the period July 1, 1949 to December 15, 1950, or seven percent of the total plane mileage operated during the entire past period through and including December 15, 1950.

Equipment

During the past period through May 28, 1950 C & S operated most of its schedules on its international system with DC-4 aircraft. In this operation the carrier averaged during the period approximately 7.6 hours per day utilization with such equipment. From May 29, 1950 through December 15, 1950 the DC-4 aircraft were utilized approximately 8.2 hours per day as well as DC-3 aircraft having a daily utilization of 8.4 hours. Even after the indicated disallowance has been made for excessive scheduling the adjusted utilization of the equipment was reasonable. We, therefore, find that the aircraft assigned to the carrier's international division were used and useful and will be recognized in their entirety for rate-making purposes.

Operating Results

While the break-even need level of C&S on a unit basis has, since the beginning of its operations, compared unfavorably with that of other carriers having similar type operations or operating in the Latin American area, the trend

in C & S's break-even need was steadily downward through June 1949. Beginning with the year ended December 31, 1949, however, and for each annual period ended with subsequent quarters C & S's break-even need trend on a unit basis was steadily increasing. This trend is shown in the following table:

Year Ended	Per Revenue Ton-Mile	Per Standard Available Ton-Mile*
	Reported Break-Even Need	
12/31/48	40.51¢	13.55¢
3/31/49	36.45	12.58
6/30/49	30.83	11.08
9/30/49	30.58	10.32
12/31/49	33.69	10.49
3/31/50	36.40	10.84
6/30/50	39.74	11.48
9/30/50	36.82	11.58

* DC-3 @ 2.4 tons; DC-4 @ 6 tons.

The relatively high level of the carrier's break-even need is in large part due to the very low traffic potential on its international system particularly that south of Havana. This is shown in Appendix No. 2 which compares the density of C & S's international system with that of seven other carriers and indicates that except for Colonial Airlines and Braniff Airways, C & S's traffic density in terms of revenue ton-miles per route mile per day was the lowest of the entire group.

The fact that the carrier's increasing break-even need after June 1949 was accompanied by relatively low unit operating expenses and declining load factors and yields indicates that revenue factors rather than unduly high operating expenses were responsible. Appendix No. 3 indicates that as the carrier increased its service volume its unit expenses on a comparative basis achieved a very low level, but that in spite of these economies its revenues declined to such an extent that break-even need nevertheless increased.

Revenues

The carrier has substantiated with factual proof its claim that over the entire period of its operations it actively resisted attempts of other carriers to reduce the general level of fares in the Caribbean area. We therefore
 125 find that it has been only as a result of C & S's attempt to meet competitive fares where necessary that its unit revenues have been steadily declining during recent years; and that therefore the level of its unit revenue yields was reasonable during the past period.

The only adjustment to operating revenues is the loss which results from the capacity disallowance previously discussed. We find, in view of the relatively constant degree of competition to which the carrier's traffic was subject, that the load factor attained by it for the year ended June 1949 (prior to the addition of the capacity found to be excessive) was a load factor reasonably attainable during the subsequent year at the same service volume. We have therefore estimated the passenger-mile volume which would have obtained without the addition of the excessive capacity during the year ended June 30, 1950, by applying the prior year's load factor to the capacity operated as of June 1949. The passenger-mile volume carried in excess of that amount is estimated as the volume which would have been lost had the excess capacity not been operated. Adjustments to reported volumes, not only of passenger-miles, but also of freight and excess baggage, are shown in Appendix No. 1.

Passenger, freight and excess baggage revenues during the past period have been reduced by \$133,000, reducing non-mail revenue from \$6,012,000, as reported by the carrier, to \$5,879,000, (Appendix No. 4) which reflects the adjustment outlined above.

Expense Adjustment for Excess Capacity

Appendix No. 4 sets forth the adjustments which have been made to the reported expense figures of C & S. The disallowance of 341,000 plane miles previously indicated

as the excessive plane miles operated during the year
 126 ended June 30, 1950 requires a reduction in the carrier's expenses. The reduction in expense in the flying operations and in the direct maintenance categories totals \$209,000 and was determined on the basis of the reported expense per revenue plane mile in these categories for the year ended June 30, 1950. The adjustment required in depreciation expense and in ground and indirect maintenance expense totals \$31,000 and was determined on the basis of the change in allocation of these expenses to the international operation. Ground operations expense as reported was reduced by \$8,000 on the basis of arrivals and departures. Passenger service expense as reported was reduced by \$15,000 on the basis of the cost per passenger-mile for the year ended June 30, 1950. Selling expenses, including traffic and sales, advertising and publicity, were reduced by \$24,000 from the reported figure for the year ended June 30, 1950 on the basis of the percentage by which non-U. S. mail revenues had been reduced from the reported figures for that year. General and administrative expense was reduced by \$26,000, the adjusted figure estimated at 8.92 percent of total adjustments excluding general and administrative expense.

The total of these expense adjustments attributable directly to the elimination of excessive capacity totalled \$313,000. As shown in Appendix No. 4, pages 2 and 3, the net adjustment to recorded break-even need resulting from the elimination of excessive capacity results in a net decrease in break-down need of \$180,000 after the revenue adjustments of \$133,000 are subtracted from the adjustments to expense.

Direct Maintenance

The only adjustment required in the direct maintenance account is to provide for amortization of the built-in overhaul for the DC-4 aircraft and engines, and the amortization of actual overhaul expenses. C & S does not
 127 have overhaul reserves and has charged overhaul costs to direct maintenance expenses as incurred.

In order to avoid cost fluctuations and in accordance with the built-in overhaul adjustments in the depreciation expense, the carrier's overhaul expenses have been reversed and capitalized and their amortization effected by spreading experienced costs over the overhaul cycle. As a result, direct maintenance expenses have been increased by \$66,000.

Depreciation—Flight Equipment

In the C & S domestic rate opinion of July 1, 1948,¹⁰ the Board recognized and capitalized a high level of DC-4 integration costs with the express condition that for purposes of mail pay determination the carrier's DC-4 depreciation expense be computed on a five-year service life rather than four years which was then considered reasonable for other carriers. C & S has not conformed with this requirement and has been depreciating its DC-4 equipment over less than four-year periods, in some cases at a service life as short as fifteen months. In accordance with our previous domestic opinion, adjustments amounting to \$425,000 are made to reflect a service life of five years and ten percent residual value.

The elimination of the built-in overhaul from the depreciable cost of DC-4 aircraft, in accordance with the Board's previous opinions on this matter, results in a decrease in depreciation expenses amounting to \$85,000 for the hulls and \$30,000 for the engines, raising the total adjustment to depreciation expenses to \$540,000.

Allocation Between Domestic and International Services

In the carrier's domestic mail rate proceeding, the revised allocation of certain common expenses between domestic and international operations, which had been
 128 effected by the carrier on January 1, 1948, was applied from the beginning of international operations on November 1, 1946.¹¹ The corresponding adjustments in

¹⁰ Chicago and Southern Air Lines, Inc., Mail Rates, 9 CAB 786, 798 (1948).

¹¹ *Supra*, Note 10.

international operating results for the period from November 1, 1946 to December 31, 1947 are: an increase of \$19,000 in ground and indirect maintenance, an equivalent decrease in advertising and publicity expense and an increase of \$33,000 in general and administrative expense.

DC-4 Integration Costs

Amortization of DC-4 developmental and training costs over a five-year period, which was provided for in the domestic mail rate proceeding, has similarly been recognized. System amortization charges were allocated to international operations in proportion to adjusted depreciation expenses. In view of the sale and retirement of the carrier's DC-4's in the latter half of 1950, amortization was accelerated in the last quarter of 1950 to absorb the remaining balance of integration costs. The amount of \$114,000 claimed by the carrier has been adjusted to eliminate charges prior to the beginning of international operations on November 1, 1946, resulting in a total allowance of \$111,000 for the review period.

Amortization of Preoperating Expense

Preoperating expenses of \$49,000 incurred by the carrier in preparing for certificated operations after the grant of its route certificate have been examined and found reasonable in nature and amount. Accordingly, their complete amortization in the review period has been allowed.

Nonoperating income and expense

Profit on the sale of the carrier's DC-4 aircraft, which were used in international operations during the review period, has been included as other income to reduce break-even need pursuant to Board policy. The profit
 129 has been calculated from the depreciated cost as adjusted to reflect application of the standard five-year life and ten percent residual value for DC-4 equipment, and elimination of "built-in overhaul" from the depreciable cost. The amount of \$19,000 has been allocated as profit to

international operations on the basis of relative depreciation charges to international and domestic operations.

The carrier has claimed \$65,000 for contingent expenses of foreign operations. This has been disallowed in conformance with the Board's established policy that unrealized and purely prospective costs may not be recognized for the purpose of determining mail rates.

Adjusted Break-Even Need

On the basis of the foregoing adjusted total expenses of \$9,001,000 and operating revenues of \$5,879,000, the carrier's break-even need is \$3,122,000 or 67.27 cents per revenue plane mile. This amount is 18.5 percent below the breakeven need of \$3,831,000 claimed by the carrier. After full consideration of the various factors affecting the operations and the break-even need for the period November 1, 1946 to December 15, 1950, we believe that the carrier's revenues and expenses, as herein adjusted, are fair and reasonable for mail pay purposes.

During the past period, 1948-1950, for which the international rate is established herein, the domestic division of C & S was operating under a final mail rate which was made effective January 1, 1948 (*Chicago & Southern Air Lines, Inc., Mail Rates*, 9 C.A.B. 786), and is currently outstanding. Over that period the domestic division earned an average return on investment estimated at 12½ percent. The level of such earnings poses the problem as to whether any portion of the revenues realized by
130 C & S under its domestic mail rate can or should be offset against the need which would otherwise be found to exist in relation to C & S's international operations, with a resulting reduction in the mail pay to be provided for such operation. We have considered the possible offset of such revenues, but we find that policy considerations to which we advert below render such offset inappropriate.

One primary objective of the Act is to further the development of the airline industry to a point where, in general, it will reach a self-sufficient status. From the mail

rate standpoint this goal is best attainable by placing carriers on permanent rates rather than on cost-plus bases for mail payments. *Transcontinental and Western Air, Inc. v. Civil Aeronautics Board*, 336 U. S. 601 (1949). For it is under permanent rates that there exists maximum incentive on the part of carriers to economical and efficient operation. This conclusion follows because, with the realization that they will retain the advantages of good earnings and yet stand any losses which may eventuate thereunder without reimbursement, carriers will, while on closed final rates, bend every effort to keen, economical, and prudent management.

The responsibility of the Board to place carriers on final future rates as rapidly as possible is an exacting one to discharge even where the carrier operates either
 131 solely in the domestic or solely in the international area. With regard to carriers comprising both domestic and international divisions, the practical problems presented in any attempt to place both divisions on final rates simultaneously are more difficult because many considerations which enter into the fixing of an international rate are different from those entering into the establishment of a domestic rate. As a practical matter, unless a permanent rate under which the carrier will bear the risks of the future can be fixed for domestic operations, where that course is feasible, without the necessity for determining simultaneously the rate for a companion international division, it may often prove to be impossible to fix any permanent rate for the carrier for an extended period of time. Indeed, if we were to determine that such rates must invariably be established simultaneously, it might well turn out to be impossible in some cases to establish future final rates at any time for carriers comprising both domestic and international divisions. Yet, the fixing of forward final rates which stimulate to the maximum the carrier's incentive to low cost operation and high revenue production cannot be foreclosed to the Board if its statutory responsibilities are to be discharged adequately.

132 The public interest in maintaining and furthering the incentive to carriers generated under forward final rates leads us to the conclusion that at this time, without review of any question of power but simply as a matter of policy, we should not offset the profits of the domestic division of C & S earned under the closed rate in establishing the mail rate for the international operation.

We find, therefore, that the principles of the Act will not be best served now by a policy of application of excess earnings under a past rate, as in the case before us, and, accordingly, that the need of the international division of C & S should not be reduced by offset of any portion of the earnings of its domestic division during the three years in issue. In this connection, of course, it should be borne in mind that although the domestic division retains the earnings experienced while on the unconditional permanent rate fixed for that division, we have it in our power, as does the Postmaster General, to institute a proceeding looking toward decrease of the rate for that division when it passes the bounds of reasonableness; and the
133 Board has exercised that power in the past.¹²

Simultaneously with the issuance of this statement, we are causing studies to be made by the staff of the earnings of C & S and of other carriers similarly situated to determine whether proceedings should not be instituted looking toward a decrease in their current final domestic mail rates.

Past Period Investment

Investment claimed by the carrier and recognized for the past period has been set forth in Appendix No. 5, together with adjustments required for rate-making purposes. The average investment claimed by C & S from the beginning of international operations to December 31, 1950
134 amounts to \$1,270,000. This sum does not vary significantly from the investment as herein adjusted, totaling \$1,360,000.

¹² A recent example is the show cause order in Pioneer Air Lines, Inc., Mail Rates, Docket No. 4000, Order Serial No. E-3010, July 14, 1949, which was finalized on September 15, 1950 by Order Serial No. E-4613.

With respect to working capital, the amount of \$508,000 claimed by the carrier has been reduced by \$35,000. In arriving at working capital investment, C&S neglected to consider all working capital components, namely, the prepayments of \$16,000 and deferred charges of \$2,000 among assets, and deferred credits of \$25,000 and operating reserves of \$6,000 among liabilities. These items when properly included effect a net reduction in working capital of \$13,000. A further reduction of \$22,000 has been made to eliminate excess mail pay from working capital as determined in this order. The resulting recognized working capital of \$473,000 is equivalent to almost three months' adjusted cash operating expenses, a level which indicates a satisfactory financial condition.

The built-in overhaul adjustments and the adjustment of DC-4 depreciation which accrued during the review period result in an average increase in the carrier's investment in flight equipment of \$201,000. This amount comprises: (a) \$183,000 arising from the adjustment of DC-4 depreciation expense to reflect the change in service life from four years and ten percent residual value to five years and ten percent residual value; and (b) \$18,000 conforming to the adjustment of operating expense for built-in overhaul costs.

In accordance with the policy of disallowing investment in equipment purchase funds for rate-making purposes, as set forth in previous cases,¹³ the amount of \$154,000, 135 representing the average amount of advance payments for the purchase of Constellation aircraft, has been removed from investment. During the review period C&S did not use the Constellation aircraft for which these funds were established, and therefore no provision for interest has been made in the past period investment.

Prepayments and deferred charges of a current nature amounting to \$18,000 have been transferred from long-term prepayments to the more appropriate category of working capital as discussed above. Additional amounts of \$25,000

¹³ Braniff Airways Mail Rates, 9 C.A.B. 607, 624 (1948);

Pan Am. Airways, Inc., Transatlantic Mail Rates, 8 C.A.B. 267, 285 (1947).

and \$71,000 have been provided herein to reflect the capitalization of preoperating costs and DC-4 integration costs, respectively, in accordance with the amortization of these items allowed in expenses.

After making the foregoing adjustments the investment recognized herein for the past period amounts to \$1,360,000 (Appendix No. 5).

Mail Rate

The break-even need for the review period, as determined on the basis of the foregoing adjustments, is \$3,122,000. In addition to this amount, the fair and reasonable mail rate must include a fair return on recognized investment. It has been the Board's consistent practice to provide a somewhat lower rate of return for past periods than for future periods in view of the fact that for past periods the probability of error in estimates of operating results is removed and operating risks have been realized. Accordingly, a return of seven percent per annum on the recognized investment of \$1,360,000 will be provided in addition to the break-even need for the review period. This return amounts to 136 \$393,000. The allowance for Federal income taxes of \$130,000 has been computed by removing revenue adjustments and deducting expense disallowances from net taxable income in accordance with the provisions of recent mail rate decisions of the Board.¹⁴

On the foregoing basis, we find that the fair and reasonable rate for the transportation of mail by aircraft over the carrier's international routes for the period November 1, 1946 through December 15, 1950, is \$3,645,000, which is equal to 78.51 cents per revenue plane mile. The mail pay of \$3,645,000 is inclusive of and not in addition to the mail compensation heretofore received by the carrier for mail transported from November 1, 1946 to December 15, 1950, inclusive.

¹⁴ Colonial Air Lines, Inc., Bermuda Mail Rates, Order Serial No. E-5065 of January 24, 1951.

Western Air Lines, Inc. and Inland Air Lines, Inc., Mail Rates, Order Serial No. E-4870 of November 24, 1950.

MAIL RATES FOR THE PERIOD ON AND
AFTER DECEMBER 16, 1950

Scheduled Service Required

The carrier estimated that 1,679,000 revenue plane miles would be flown during a future year. This estimate is based upon a daily round trip between Houston and New Orleans with DC-3 aircraft which amounts to an annual total of 219,000 revenue miles, and the daily operation of Constellation equipment over the New Orleans-Havana-Kingston-Caracas segment totaling 1,460,000 annual revenue miles.

On December 16, 1950 the carrier initiated the operation of Constellation equipment on its international routes, substituting this aircraft on all its former DC-4 schedules. As we pointed out in the section related to the past period, the traffic on the segments south of Havana did not justify the maintenance of daily service over this portion of the route after a reasonable experimental period. This situation is

aggravated by the use of the larger and more modern
137 equipment which the carrier indicates is necessary
for competitive reasons. While we realize that competition is encountered on the Havana-Caracas segment, there appears to be no compelling reason to warrant the recognition of seven weekly round-trips with Constellation aircraft. In particular, the load factors experienced on this segment in the year 1950 in the operation of seven weekly round-trips with DC-4 aircraft, hardly justify continuing these schedules with Constellation equipment.

We find, therefore, that four round trips per week Havana-Kingston-Caracas with Constellation aircraft is a reasonable volume of service on this segment for a future year. The elimination of 413,000 miles applicable to the three additional round trips per week estimated by the carrier results in 1,047,000 revenue miles to be recognized for the Constellation operation. This mileage, added to the 219,000 miles to be flown with DC-3 aircraft, brings the total revenue plane miles to be recognized for a future year to 1,266,000.

On the basis of the revenue miles recognized above and the standard capacities of 21 seats and 2.4 tons for DC-3 aircraft and 52 seats and 8.0 tons for Constellation equipment, the available seat-miles and available ton-miles to be recognized for the future year are 59,043,000 and 8,902,000, respectively (Appendix No. 6).

In view of the competitive routings which exist for passengers traveling from the United States to Kingston and Caracas, it is reasonable to expect that the reduction which we have made in the carrier's service to and from these points will result in a reduction in the carrier's ability to generate traffic. Consequently, the carrier's estimate of 31,100,000 revenue passenger-miles to be carried in the future year has been adjusted to reflect the indicated decrease in the capacity to be recognized. Since we have reduced

the service to be recognized by 3/7ths between Havana and Caracas a reasonable reduction in the passenger traffic estimate for Kingston and Caracas passengers appears to be a decrease of 2/7ths. This estimate of a 2/7ths reduction is necessarily based on judgment since we are unaware of any exact method by which to determine the decline in passenger traffic resulting from a reduction in capacity to be operated. To the extent that the estimated decline is not directly proportional to the curtailment of capacity, it is our view that this is a reasonable estimate since even the recognized capacity after reduction exceeds what might be termed a minimum pattern of service for the Havana-Caracas segment.

The 2/7th reduction in passenger traffic has been applied to all traffic originated or terminated at Kingston and Caracas except for the local Caracas-Havana traffic which can be carried by C&S only on three schedules per week. Applying the 2/7th reduction to the traffic estimated with the single exception noted, we have recognized a decrease of 5,200,000 revenue passenger-miles from the total estimated by the carrier for a future year. This results in a net to be carried by C&S of 25,900,000 revenue passenger-miles and results in a passenger load factor for the future year

of approximately 44 percent for the entire international route.

Freight ton-miles have been estimated at 533,000 on the basis of the freight revenue forecast for the future year and the freight yield per ton-mile estimated by the carrier.

Excess baggage ton-miles and foreign mail ton-miles have been estimated by dividing the estimated revenue in each category by the yield per ton-mile experienced during the third quarter of 1950, which results in 90,000 excess baggage ton-miles and 3,000 foreign mail ton-miles.

The U. S. mail ton-miles have been forecast at 23,000 for the future year by applying the average load experienced during the third quarter of 1950 to the estimated miles to be flown.

139 *Non-U. S. Mail Revenues*

The carrier estimates \$2,411,000 in passenger revenues for a future year as set forth in Appendix No. 7. An adjustment of this amount is necessary to reflect the reduction in passenger-miles attributable to the reduced volume of service which has been found adequate to meet the needs of the traffic.

Since the Kingston and Caracas traffic produce higher passenger yields than realized elsewhere on the carrier's route, it is necessary that the traffic be eliminated on these segments at a yield higher than the average passenger yield of 6.77 cents forecast by the carrier. A yield of 7.50 cents per passenger-mile, representing the estimated average yield of the passenger traffic to Venezuela, was used in determining the passenger revenue lost due to reduction in Caracas traffic, and 7.00 cents per passenger-mile was used for the loss of Kingston traffic. The passenger revenue forecast by the carrier has thus been reduced by \$385,000 leaving an adjusted amount of \$1,720,000 or 6.64 cents per passenger-mile.

The excess baggage revenue of \$74,000 estimated by the carrier has been adjusted to \$60,000 in order to retain the relationship to passenger revenue indicated in the carrier's forecast.

The freight revenue forecast by the carrier is \$205,000 or 12 cents per revenue mile. Applying this yield per revenue mile to the revenue miles estimated for the future results in \$152,000 of freight revenue for the future year.

Foreign mail revenue for a future year which was estimated at \$8,000 by the carrier has been revised to \$7,000, based upon the level of other revenues. The estimate of \$19,000 in other non-U.S. mail revenues forecast by the carrier has been accepted as reasonable.

140 *Total Non-U.S. Mail Revenue*

The total non-U.S. mail revenues, which were estimated by the carrier to be \$2,411,000, have been reduced by \$453,000 to reflect the adjustments in the various categories discussed above. Therefore, the adjusted estimate of total non-U.S. mail revenues is \$1,958,000.

Operating Expenses

We have used the adjusted expenses for the year ended June 30, 1950 as the base year for estimating future expenses, and have made allowances for increased costs which became effective in 1950 but were not fully reflected in the base year. The bases for future year estimates have been detailed by account in Appendix No. 7.

In forecasting flying operations expense for a future year, we have applied the carrier's estimated cost of 28.29 cents per DC-3 revenue plane mile to its projected DC-3 mileage, and its estimated cost of 69.05 cents per revenue plane mile of Constellation operation to the adjusted mileage for this operation. Likewise, DC-3 direct maintenance expense represents application of the carrier's cost estimates of 10.04 cents per revenue plane mile. Direct maintenance expenses of Constellation aircraft have been estimated at 35.00 cents per plane mile. Depreciation claimed by C & S has been adjusted to reflect adoption of the standard 7-year life and 10 percent residual value for Constellation equipment in place of the 5-year life proposed by the carrier. These adjustments effect a reduction of \$575,000

in the carrier's estimated aircraft operating expenses and result in a recognized total of \$1,473,000 for a future year.

The carrier's forecast of ground and indirect expenses has been found reasonable after downward adjustments of three expense categories. Passenger service expense,

141 taken at the carrier's unit cost of 0.926 cent per revenue passenger mile, has been reduced to agree with the adjusted revenue passenger-miles. Traffic and sales and advertising and publicity expense claimed by the carrier has been reduced to an amount aggregating 20 percent of estimated non-U.S. mail revenues, a ratio approximating that established for comparable carriers in recent rate cases; and on the basis of a similar comparison, general and administrative expense has been reduced to an amount representing 10 percent of other cash expenses. These adjustments, totaling \$266,000, result in adjusted ground and indirect expenses of \$1,821,000.

Total operating expense for a future year has thus been found to be \$3,294,000, equivalent to 260.25 cents per revenue plane mile. This is a high level of expense, but represents the summation of costs which have been individually examined and found reasonable, and is 20 percent below the carrier's estimate. As indicated in the foregoing discussion, the high cost is primarily due to the introduction of Constellation aircraft to enable the carrier to maintain its competitive position and to coordinate with Constellation service on its domestic system. The inherently high unit cost of operating this equipment over the international route, with its relatively low traffic density, has been weighed with regard for these factors. The influence of the general rise in material and labor costs being experienced has also been taken into account. After consideration of the particular circumstances of the carrier's situation, the stated amount of its future year operating expenses has been recognized.

Break-Even Need

The adjusted break-even need for the future year based on non-U.S. mail revenues of \$1,958,000 and total expenses of \$3,294,000 is \$1,336,000, equal to \$1.06 per revenue plane mile.

142 *Investment*

The recognized investment allocated to the international operations for the future period is based on the preliminary balance sheet as of December 31, 1950, which has been adjusted to reflect the elimination of amounts not recognized for rate-making purposes. These adjustments have been summarized in Appendix No. 8.

The total future investment claimed by C & S amounts to \$3,044,000. Of this total \$916,000 represents net working capital based upon the carrier's estimate of three months' cash operating expenses. As of December 31, 1950, however, the carrier's working capital allocated to international operations amounted to \$468,000 after the inclusion of \$104,000 representing 26.30 percent of \$397,000 obtained from the sale of two DC-4 aircraft during the first quarter of 1951. The ratio of 26.30 percent which has been used to allocate working capital between domestic and international operations represents the relationship of estimated cash operating expenses for international operations to the total cash operating expenses of the entire C & S system. From the total working capital of \$468,000 we have deducted \$193,000 which is the international portion of the excess mail pay received by C & S during the review period. The net resulting working capital as herein determined for rate purposes amounts to \$275,000.

Since all Constellation equipment is used by C & S on a system basis, the carrier estimates that one-third of the common investment in six Constellation aircraft should be allocated to international operations. This allocation on the basis of revenue plane miles estimated for the future period appears reasonable and is recognized in the future investment. As indicated in Appendix No. 8, the investment in

Constellation equipment, after restoring the book value of the aircraft to the level of December 16, 1950, is 143 \$2,334,000 or one-third of \$7,000,000, the approximate total cost of six Constellations. To this amount is added \$9,000 representing capitalized interest on the equipment purchase funds relative to these aircraft.

Prepaid and deferred items of a current nature, claimed by the carrier as part of its fixed assets have been eliminated and provided for in working capital. Long term operating property prepayments of \$24,000, the same amount reported in 1950, are found reasonable and are so included in future investment. An additional \$83,000 claimed by the carrier for this category of investment does not appear to be adequately supported and is herein disallowed for rate-making purposes. After all adjustments, the net decrease to claimed investment is \$294,000 resulting in recognized investment of \$2,750,000.

Determination of Mail Rates

In accordance with our findings discussed previously herein, we have determined C & S break-even mail pay requirements to be \$1,336,000 equal to \$1.06 per revenue plane mile as forecast. This determination is \$388,000 or 22.51 percent lower than the break-even of \$1,724,000 estimated by the carrier. The acquisition of the Constellation aircraft has expanded the investment base so that application of a ten percent rate of return, which we have consistently considered fair and reasonable for international operations in a future period, produces a return element of \$275,000 equal to 21.72 cents per revenue plane mile. This compares with an average of 8.36 cents per mile recognized in the past period. Provision for federal income taxes at 47 percent results in the amount of \$244,000 equal to 19.27 cents per revenue plane mile. Total mail pay requirements are, therefore, \$1,855,000 or \$1.47 per revenue plane mile flown in scheduled service.

144 The mail pay requirement of C&S for the future is at a higher rate than any of those currently in

effect for other international carriers. It exceeds the requirement of the other carriers by a substantial margin on any of the customary bases of mail pay comparison, such as plane miles, mail ton-miles or as a percentage of total revenue.

As indicated above, this relatively high level of mail pay, brought about by the operation of Constellation aircraft over a route of very low traffic density, is justified by the circumstances peculiar to C&S operation.

The very fact that the rate established for the future period is substantially higher than that found appropriate for the past period necessarily raises the question whether some adjustment of the route pattern and the volume of services provided south of Havana may not be required. We do not imply by this statement that an adjustment in C&S's route south of Havana is required since, in addition to C&S, operations south of Havana are conducted by other American flag carriers as well as foreign air carriers. However, the high level of mail pay for C&S indicates that it may be appropriate to examine the route structure under which international service south of Havana is being provided by the United States carriers in general, for the purpose of determining whether a realignment of routes in that area might result in reducing the dependency upon the United States Government for mail pay support without a corresponding reduction in the quality of such services. Accordingly, while we do not intimate any definite view as to whether such a realignment may or may not be proper, we have instructed the staff to include the Caribbean area for scrutiny along with the present studies of the domestic route structures. If, upon completion of such studies action with regard to such structure appears warranted, we shall then take such action by formal order and proceeding.

145 C & S has requested a mail rate formula which will provide mail compensation in accordance with our determination on the basis of estimated available seat-miles flown. In view of the carrier's request, we will establish for the period on and after December 16, 1950 a rate which

is calculated to produce the annual amount of mail pay prescribed herein, will be reasonable in terms of the schedule pattern recognized in this opinion, and will change in relation to fluctuations in the volume of service which may be offered.

In order to insure that C & S will receive the amount of mail pay intended by our order, to provide an effective safeguard against overpayment by reason of schedules operated in excess of those found to be required, and finally to distribute mail pay evenly from month to month throughout the year, the recognized available seat-miles over a four-week or twenty-eight day period will be used as a base monthly standard available seat mileage. Accordingly, a base rate of 3.41 cents per standard available seat-mile with a maximum monthly capacity of 4,529,000 standard available seat-miles is found to be the fair and reasonable mail rate for the period on and after December 16, 1950.

CONCLUSION

On the basis of the foregoing considerations, we find that the fair and reasonable rates of compensation to be paid to C & S for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith between the points on its Latin American routes between which the carrier is presently or hereafter may be authorized to transport mail by its certificates of convenience and necessity are as follows:

- 146 A. For the period November 1, 1946—December 15, 1950, inclusive, the sum of \$3,645,000.¹⁵

¹⁵ This amount is equivalent to a rate of 78.51 cents per recognized revenue plane mile flown in scheduled service over the international system. For administrative purposes, the breakdown of mail compensation by periods is as follows:

November 1, 1946—December 31, 1946	152,000
January 1, 1947—June 30, 1947	291,584
July 1, 1947—December 31, 1947	296,416
January 1, 1948—June 30, 1948	358,032
July 1, 1948—December 31, 1948	361,968
January 1, 1949—June 30, 1949	539,032
July 1, 1949—December 31, 1949	547,968
January 1, 1950—June 30, 1950	544,488
July 1, 1950—December 15, 1950	553,512
Total	3,645,000

B. For the period on and after December 16, 1950:

For each calendar month an effective rate per designated mile flown obtained by dividing by the designated miles flown during the month the product of 3.41 cents times the lower of 4,529,000 or the standard available seat-miles flown in scheduled passenger service during the month. For the period from December 16, 1950 to December 31, 1950, the mail rate shall be derived by dividing by the designated miles flown therein the product of 3.41 cents times the lower of 2,264,500 or the standard available seat-miles flown in scheduled passenger service during the period.

The available seat miles flown in scheduled passenger service during the month shall be computed by multiplying the scheduled mileage flown in passenger service during the month with each aircraft type by the standard available seats for that type as specified below:

Aircraft Type	Seats
DC-3	21
DC-4	44
Constellation	52

The aforesaid rates per airplane mile shall be applied to, and the designated mileage flown shall be computed on, the direct airport-to-airport mileage between points served for the carriage of mail on each trip flown on a schedule
 147 designated or ordered to be established by the Postmaster General for the carriage of mail, and the scheduled mileage flown shall be computed on the direct airport-to-airport mileage between points actually served on each trip flown in scheduled passenger service, including all trips operated as extra sections thereto.

The compensation provided above should be inclusive of, and not in addition to, the mail compensation received by the carrier for the transportation of mail on and after November 1, 1946 over its Latin American routes.

An appropriate order will be entered.

CHICAGO AND SOUTHERN AIR LINES, INC.—INTERNATIONAL

Traffic Statistics as Reported and as Adjusted
For the Period November 1, 1946–December 15, 1946

	11-1-46 to 6-30-49	As Reported 7-1-49 to 12-15-50
<i>Capacity Operated (000)</i>		
Revenue plane miles	2,072	2,912
Available seat-miles—reported	96,416	119,917
—standard ²	90,778	125,356
Available ton-miles—reported	10,586	14,958
—standard ³	12,385	17,038
<i>Capacity Utilized (000)</i>		
Revenue passenger-miles	33,860	40,113
Revenue ton-miles:		
Passenger (@ 215 lbs.)	3,641	4,312
Freight	374	804
Excess baggage	102	146
Foreign mail	2	8
U. S. mail	12	42
Total	4,131	5,312
<i>Load Factors (Percent)</i>		
Passenger—reported	35.12	33.45
—standard	37.30	32.00
Over-all—reported	39.02	35.51
—standard	33.35	31.18
Average daily route miles in operation	1,247	2,321
Revenue ton miles per route mile per day	3.40	4.29
Average daily round trip frequency	.85	1.18
Average daily revenue hours per aircraft	6.8	8.9
Performance factor (percent)	96.91	99.51
<i>Revenue per Unit of Service (Cents)</i>		
Passenger revenue per rev. pas.-mile	7.55	7.17
Revenue per ton-mile:		
Passenger	70.23	66.74
Freight	35.96	27.91
Excess baggage	61.51	71.88
Foreign mail	200.00	200.00

¹ Scheduled and nonscheduled operations.

² Standard capacities: DC-3, 21 seats; DC-4, 44 seats.

³ Standard available tons: DC-3, 2.4 tons; DC-4, 6 tons.

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONS

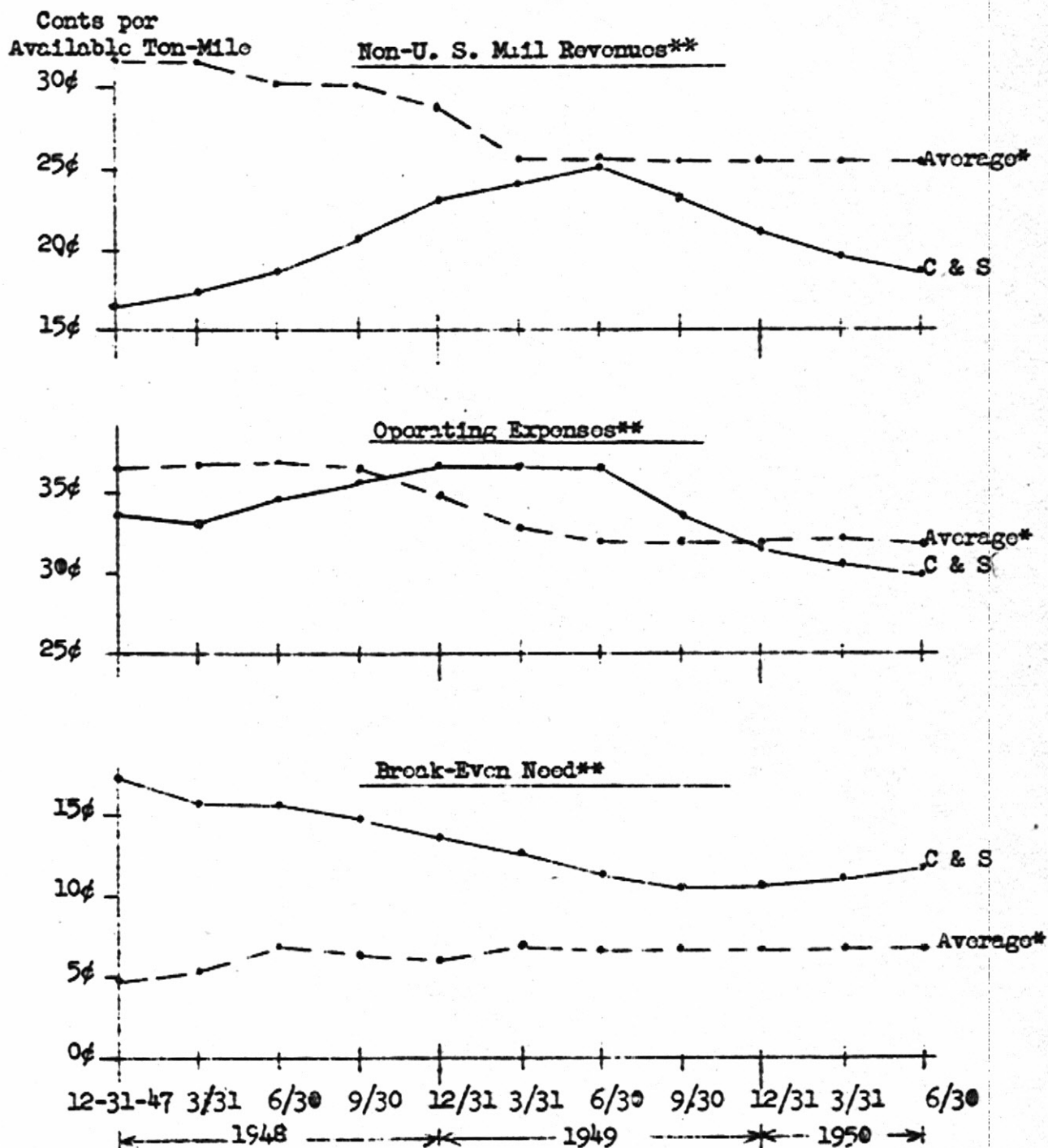
Comparisons of Traffic Density with Other Carriers

U. S. Flag International Carrier	Revenue Ton-Mile per Route Mile per Day Year Ended	
	Sept. 30, 1949	Sept. 30, 1950
Pan American—LAD	17.4	17.8
AAL—Mexico	14.5	15.2
NAL—Havana	11.4	14.8
Panagra	5.7	6.1
EAL—San Juan	5.7	5.9
Chicago and Southern	4.1	4.1
Colonial	3.3	4.7
Braniff	1.7	2.0

CHICAGO AND SOUTHERN AIR LINES, INC. - INTERNATIONAL OPERATIONS

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Comparison of Revenues, Expenses and Break-Even Need
with that of Other U. S. Flag Carriers
per Standard Available Ton-Mile
(12-month moving totals)



* Arithmetic average of international operations of American, Braniff, Colonial, Eastern, National, Panagra and Pan American's Latin American Division.

** Per standard available ton-mile.

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONS

Financial Results as Claimed and as Adjusted for the Period
November 1, 1946—December 15, 1950
(in thousands)

	Claimed by the Carrier ¹	Adjust- ments	As Adjusted Amount	Cents per Rev. Mile
Revenue plane miles	4,984	-341	4,643	—
<i>Non-U. S. Mail Revenues</i>				
Passenger	\$5,435	\$-120 D	\$5,315	114.48
Excess baggage	168	-4 D	164	3.53
Express	—	—	—	—
Freight	359	-9 D	350	7.54
Foreign mail	20	—	20	.43
Other non-U. S. mail	30	—	30	.65
Total Non-U. S. Mail Revenues	\$6,012	\$-133	\$5,879	126.63
<i>Operating Expenses</i>				
Flying operations	\$2,285	\$-155 D	\$2,130	45.88
Direct maintenance—flight equipment	962	12 A D	974	20.98
Depreciation—flight equipment	1,250	-562 B D	688	14.82
Total Aircraft Operating Expenses	\$4,497	\$-705	\$3,792	81.68
Ground operations	\$1,646	\$ -8 D	\$1,638	35.30
Ground and indirect maintenance	636	9 C D	645	13.88
Passenger service	614	-15 D	599	12.90
Traffic and sales	1,081	-43 C D	1,350	29.08
Advertising and publicity	312			
General and administrative	768	7 C D	775	16.69
Depreciation—ground equipment	79	—	79	1.71
Total Ground and Indirect Expenses	\$5,136	\$ -50	\$5,086	109.56
Total Operating Expenses	\$9,633	\$-755	\$8,878	191.24
Profit on sale of DC-4 aircraft ²	\$ —	\$ -19 G	\$ -19	-0.41
Amortization of DC-4 integration costs	114	-3 E	111	2.40
Amortization of preoperating expenses	49	—	49	1.06
Nonoperating income and expenses ²	47	-65 F	-18	-0.39
<i>Break-Even Need</i>	\$3,831	\$-709	\$3,122	67.27

¹ Non-U. S. mail revenues and operating expenses as reported on Form 41 except for data for period 7-1-50 to 12-15-50 which were submitted by the carrier as special information. Other data as claimed by carrier.

² Minus sign indicates income.

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*Explanatory Notes**A. Direct Maintenance*

- | | |
|---|-----------|
| 1. To eliminate aircraft overhaul expenses | \$-65,908 |
| 2. Allowance for amortization of "built-in" aircraft overhaul | 101,799 |
| 3. Allowance for amortization of "built-in" engine overhaul | 30,129 |

Total	\$ 66,020
-------	-----------

B. Depreciation—Flight Equipment

- | | | |
|---|-----------|------------|
| 1. Elimination of value of "built-in" overhaul from DC-4 aircraft and engines: | | |
| Aircraft | \$-85,195 | |
| Engines | -30,459 | \$-115,654 |
| 2. Adjustment of reported DC-4 flight equipment depreciation expense to reflect changes in service life to 5 years, 10 percent residual value | | -424,530 |

Total	\$-540,184
-------	------------

C. Revision in Allocation Bases

To reduce reported domestic operating expenses and increase reported international expenses for the period November 1, 1946 to December 31, 1947. (Order No. E-1740 of 7-1-48) The categories of cost allocations which have been revised are:

- | | | |
|------------------------------------|-----------|----------|
| 1. Ground and indirect maintenance | \$ 18,666 | |
| 2. Advertising and publicity | -18,666 | |
| 3. General and administrative | 32,666 | \$32,666 |

D. Elimination of Estimated Revenue and Expenses Applicable to the Excess Capacity

- | | |
|--|-----------|
| 1. Passenger revenue allocated on the basis of passenger-miles and average yield per passenger-mile for the year ended June 30, 1950 | \$120,523 |
| 2. Freight and excess baggage allocated on the basis of relationship to passenger revenue for the year ended June 30, 1950 | 12,800 |

Total revenue adjustments	\$133,323
---------------------------	-----------

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- | | |
|--|------------|
| 3. Flying operations expense estimated on basis of cost per revenue plane mile for the year ended June 30, 1950 | \$-155,325 |
| 4. Direct maintenance expense estimated on basis of cost per revenue plane mile for the year ended June 30, 1950 | -54,062 |
| 5. Depreciation expense as adjusted for extension of service life. This adjustment reflects only the change in DC-4 depreciation allocated to international operations | -21,508 |
| 6. Ground operations expenses estimated on basis of arrival and departures | -7,879 |
| 7. Ground and indirect maintenance. This adjustment reflects the change in the allocation between domestic and international operations | -10,149 |
| 8. Passenger service estimated on the basis of cost per passenger mile for the year ended June 30, 1950 | -14,939 |
| 9. Traffic, sales, advertising and publicity. Reasonable estimate based on the level of the other adjustments | -24,000 |
| 10. General and administrative expenses. Estimated at 8.92 percent of total adjustments excluding G & A | -25,677 |

Total expense adjustments	\$-313,539
---------------------------	------------

11. Net adjustment to break-even need		\$-180,216
		<u><u> </u></u>
E. <i>Integration Costs</i>		
International proportion of amortization of DC-4		
integration costs:		
Claimed by carrier	\$114,655	
Allowed herein	<u>111,332</u>	
Adjustment		<u>\$ -3,323</u>
		<u><u> </u></u>
F. <i>Nonoperating Income and Expenses</i>		
To eliminate provision for foreign operations contingencies		<u>\$-65,000</u>
		<u><u> </u></u>
G. <i>Profit on Sale of DC-4 Aircraft</i>		
Profit on sale of DC-4 aircraft allocated to international operations		<u>\$-19,000</u>
		<u><u> </u></u>

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONS

Average Investment as Claimed and as Adjusted for the Period
November 1, 1946—December 15, 1950
(in thousands)

	As Claimed by C. & S	Adjust- ments	As Adjusted
<i>Working Capital</i>			
Current assets	\$829	\$-22 A	\$807
Prepayments	—	16 A	16
Deferred charges	—	2 A	2
Total	\$829	\$- 4	\$825
Current liabilities	\$321	—	\$321
Deferred credits	—	\$ 25 A	25
Operating reserves	—	6 A	6
Total	\$321	\$ 31	\$352
Net working capital	\$508	\$-35 A	\$473
<i>Operating Property and Equipment</i>			
Flight equipment—net	479	201 B	680
Ground property and equipment—net	70	—	70
<i>Other Assets</i>			
Investments and special funds	172	-154 C	18
Prepaid and deferred items	41	-18 D	23
Capitalized preoperating expenses	—	25 E	25
Capitalized DC-4 integration expenses	—	71 F	71
Total Investment	\$1,270	\$ 90	\$1,360

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Explanatory Notes

- A. (1) To include in the computation of average work-capital all prepaid and deferred items of a current nature
- | | | |
|---------------------------------|-----------|-----------|
| Prepayment and deferred charges | \$ 17,845 | |
| Deferred credits | -25,118 | |
| Operating reserves | -6,453 | \$-13,726 |
- (2) To eliminate 21.71 percent of average international excess mail pay
- | | |
|--|---------|
| | -21,617 |
|--|---------|
- Total
- | | |
|--|-----------|
| | \$-35,343 |
|--|-----------|
- B. (1) To adjust the reserve for depreciation of DC-4 flight equipment to reflect change in service life
- | | |
|--|-----------|
| | \$182,687 |
|--|-----------|
- (2) To decrease reserve for depreciation of DC-4 aircraft and engines to conform to built-in overhaul adjustments of reported depreciation expense
- | | | |
|----------|----------|--------|
| Aircraft | \$37,937 | |
| Engines | 13,210 | 51,147 |

(3) To adjust for the unamortized balance of capitalized aircraft and engine overhaul expense to conform to overhaul expense adjustments of reported direct maintenance expense		-33,010
Total		<u>\$200,824</u>
C. To exclude equipment purchase funds allocated to international operations		<u>\$-153,750</u>
D. To exclude working capital items (prepayments and deferred charges) from long-term operating property prepayments		<u>\$-17,845</u>
E. Average unamortized balance of capitalized preoperating expenses		<u>\$ 24,589</u>
F. Average unamortized balance of capitalized DC-4 integration expenses		<u>\$ 71,229</u>

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Appendix No. 6

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONSTraffic Statistics as Estimated by the Carrier and as
Adjusted by the Staff for a Future Year

<i>Capacity (000)</i>	Carrier's Estimate	As Adjusted Amount	Basis
Revenue plane miles:			
DC-3	219	219	
L-649	1,460	1,047	
	<u>1,679</u>	<u>1,266</u>	A
Available seat-miles—carrier basis	77,593 ¹	0	
Available seat-miles—standard	80,519	59,043	B
Available ton-miles—standard	12,204	8,902	C
<i>Capacity Utilization (000)</i>			
Revenue passenger-miles	31,100	25,900	D
Revenue ton-miles:			
Passenger (@ 215 lbs.)	3,343	2,785	E
Freight	720	533	F
Excess baggage	111 ²	90	G
Foreign mail	4 ²	3	G
U. S. mail	31 ³	23	H
Total	<u>4,209</u>	<u>3,434</u>	
<i>Load Factors (percent)</i>			
Passenger—carrier basis	40.08		
Passenger—standard basis	36.28	43.87	
Over-all—standard basis	34.49	38.58	
<i>Revenue per Unit of Service (cents)</i>			
Passenger revenue per revenue pass.-mile	6.77	6.64	
Revenue per ton-mile:			
Passenger	62.97	61.76	
Freight	28.50	28.50	
Excess baggage	66.37	66.37	
Foreign mail	226.00	226.00	

¹ Based upon DC-3, 21 seats and L-649, 50 seats.² Carrier's estimated revenue divided by the yield per ton-mile experienced during the third quarter 1950.³ Experience during third quarter 1950 projected to annual basis.

- A. Based upon seven round trips per week Houston-New Orleans with DC-3; seven weekly round trips New Orleans-Havana and four weekly round trips Havana-Kingston-Caracas with L-649.
- B. Based upon 21 seats per DC-3 aircraft and 52 seats per L-649 aircraft.
- C. Standard capacities DC-3, 2.4 tons; L-649, 8 tons.
- D. Revenue passenger-miles estimated by the carrier have been adjusted by reducing the estimated traffic to and from Caracas and Kingston by 2/7 (28.6%) to reflect the 3/7 reduction (from 7 to 4 weekly flights) in scheduled service to be recognized to these two points.
- E. Estimated revenue passenger-miles multiplied by 215 lbs. converted to ton-miles.
- F. Estimated express revenue divided by the yield per ton-mile estimated by the carrier.
- G. Estimated revenue divided by the yield per ton-mile experienced July-September 1950.
- H. Average load experienced during the third quarter 1950 applied to estimated miles.

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Appendix No. 7

CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONSFinancial Results for a Future Year
As Estimated by the Carrier and as Adjusted
(in thousands)

	Carrier's Estimate	Adjust- ments	Adjusted Estimate Amount	Cents per Rev. Mile
Revenue Plane Miles	1,679	-413	1,266	—
<i>Non-U. S. Mail Revenues</i>				
Passenger	\$2,105	\$-385	\$1,720 A	135.90
Excess baggage	74	-14	60 B	4.74
Express	—	—	—	—
Freight	205	-53	152 C	12.01
Foreign mail	8	-1	7 D	0.55
Other non-U. S. mail	19	—	19 E	1.50
Total Non-U. S. Mail Revenues	\$2,411	\$-453	\$1,958	154.70
<i>Operating Expenses</i>				
Flying operations	\$1,070	\$-285	\$ 785 F	62.02
Direct maint.—flight equip.	532	-144	388 G	30.66
Depreciation—flight equip.	446	-146	300 H	23.70
Total Aircraft Operating Exp.	\$2,048	\$-575	\$1,473	116.38
Ground operations	\$ 626	\$ —	\$ 626 E	49.46
Ground and indirect maintenance	268	—	268 E	21.17
Passenger service	288	-48	240 I	18.96
Traffic and sales	472	-192	392 J	30.97
Advertising and publicity	112			
General and administrative	296	-26	270 K	21.33
Depreciation—ground equipment	25	—	25 E	1.98
Total Ground and Indirect Exp.	\$2,087	\$-266	\$1,821	143.87
Total Operating Expenses	\$4,135	\$-841	\$3,294	260.25
Break-Even Need	\$1,724	\$-388	\$1,336	105.55

Explanatory Notes

- A. Estimated revenue passenger-miles times 6.64 cents, estimated average yield per passenger-mile.
 B. Relationship of excess baggage revenue to passenger revenue estimated by carrier.
 C. Estimated revenue ton-miles times 28.50 cents, estimated average yield per freight ton-mile.
 D. Reasonable estimate based on level of other revenue items.
 E. As estimated by Chicago and Southern.
 F. Cost per revenue plane mile estimated by the carrier.
 G. 1. DC-3 based on cost per revenue plane mile estimated by Chicago and Southern.
 2. L-649 cost per revenue plane mile estimated at 35.00 cents per mile.
 H. Annual depreciation of two L-649 aircraft.
 I. Cost per passenger-mile estimated by Chicago and Southern.
 J. Estimated at 20 percent of non-U. S. mail revenues.
 K. Estimated at 10 percent of other cash expenses.

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161CHICAGO AND SOUTHERN AIR LINES, INC.
INTERNATIONAL OPERATIONSFuture Period Investment
(in thousands)

	As Claimed by C & S	Adjust- ments	As Adjusted
<i>Net Working Capital</i>	\$ 916	\$-641 A	\$ 275
<i>Operating Property and Equipment</i>			
Flight equipment—net	1,887	456 B	2,343
Ground property and equipment—net	74	—	74
<i>Other Assets</i>			
Investments and special funds	34	—	34
Prepaid and deferred items	26	-26 C	—
Long-term operating property prepayments	107	-83 D	24
Total Investment	\$3,044	\$-294	\$2,750

Explanatory Notes

A. (1) To reverse carrier's claimed working capital estimate	\$-916,000
(2) To provide for net working capital based upon 26.30 percent of preliminary balance sheet data as of December 31, 1950:	
Current assets	\$928,407
Prepayments	26,752
Deferred charges	4,330
Total	\$959,489
Current liabilities	\$584,140
Operating reserves	11,835
Total	\$595,975
Net working capital	363,514
(3) To reduce working capital by 26.30 percent of excess mail pay	-192,779
(4) To increase working capital to include receipts from sale of two DC-4 aircraft during the first quarter of 1951 (26.30% of \$397,000)	104,411
Total	\$-640,854
B. (1) To add first year accrued depreciation to restore book value of aircraft to the level at the beginning of L-649 opera- tions	\$446,667
(2) To provide for the capitalization of interest on equipment purchase funds at the rate of five percent per annum for a period of six months, with one-third of the total allo- cated to international operations	9,375
Total	\$456,042
C. To exclude working capital items from "Other Assets"	\$-26,321
D. To eliminate unsupported long-term operating property prepay- ments	\$-83,031

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Orders
Serial Number E-5385

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
Washington, D. C.

Adopted by the Civil Aeronautics Board at its office in
Washington, D. C. on the 18th day of May, 1951.

Docket No. 2564

In the matter of the compensation for the transportation
of mail by aircraft, the facilities used and useful there-
for, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.

over its Latin American Route.

Order to Show Cause

The Board having considered all of the information and data set forth, or specifically referred to, in the Statement of Tentative Findings and Conclusions, together with the Appendixes attached thereto, dated May 18, 1951, (hereinafter referred to as the "Statement"), which Statement is attached hereto and made a part hereof, and having on the basis thereof made the tentative findings and conclusions set forth in the Statement;

IT IS ORDERED, That Chicago and Southern Air Lines, Inc. is directed to show cause why the Board should not make final the findings and conclusions set forth in the Statement, and upon the basis thereof fix, determine and publish the rates set forth in said Statement as the fair and reasonable rates of compensation to be paid the carrier for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith over its Latin American routes on and after November 1, 1946;

IT IS FURTHER ORDERED, That all further procedure herein shall be in accordance with Section 302.13 of the Procedural Regulations and that any notice, as provided for in para-

graph (c)(1) of said Section 302.13, that there exists any objection to the rates set forth in the Statement or to the admissibility in evidence of any exhibits accompanying, or to the information specifically referred to in, the Statement shall be filed with the Civil Aeronautics Board within ten days after the date of service of this Order, and if notice is filed as aforesaid, written answer and any supporting documents, as provided for in paragraphs (c)(1) and (c)(2) of said Section 302.13, shall be filed with the Board within thirty days after the date of service of this Order;

IT IS FURTHER ORDERED, That if answer is filed
 163 hereto all elements entering into the determination of fair and reasonable rates, except insofar as limited in prehearing conference, shall be in issue, and in such event the final rates shall be determined upon the record made with respect to such issues;

IT IS FURTHER ORDERED, That this order and the attached Statement of Tentative Findings and Conclusions be served upon Chicago and Southern Air Lines, Inc.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN

M. C. Mulligan
Secretary

(SEAL)

* * * * *

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2564

CHICAGO AND SOUTHERN AIR LINES, INC.
LATIN AMERICAN OPERATIONS

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith.

Decided: October 18, 1951

For policy reasons the Board will not offset the excess earnings realized from Chicago and Southern's domestic operations under a final mail rate against the carrier's "need" for mail pay resulting from operations over its Latin American route.

Provision for Federal income taxes should be based on the actual Federal income tax rate rather than the 38 percent tax rate in force prior to the current national defense emergency.

APPEARANCES:

R. S. Maurer, L. E. Black, and W. C. Stone for Chicago and Southern Air Lines, Inc.

Roy C. Frank and Eugene J. Brahm for the Post Office Department.

Arnold D. Berkeley and Allen C. Lande, Bureau Counsel.

Opinion

BY THE BOARD:

This proceeding involves the determination of final mail rates for the Latin American operations of Chicago and Southern Air Lines, Inc., hereinafter called C&S. In re-

sponse to the petition of the carrier filed on October 11, 1946, we issued a Statement of Tentative Findings and Conclusions on May 18, 1951 (Order Serial No. E-5385),
proposing final mail rates for the international opera-
247 tions of C&S for the past period November 1, 1946-
December 15, 1950, inclusive, and for the future pe-
riod beginning December 16, 1950.

C&S has accepted the proposed rates, but the Postmaster General has filed objections and an Answer to the Statement of Tentative Findings and Conclusions. In accordance with the Procedural Regulations the issues raised by the objections have been defined and hearing has been held. The parties have submitted briefs to the Board, and have agreed to waive further procedural steps prior to final decision.

The parties have stipulated that no facts are in controversy and have submitted only two issues involving questions of policy and law for our decision. As expressly limited by agreement of the parties, the two issues are as follows:

1. Whether in fixing mail rates for past and future rate periods involving operations of C&S over its Latin American route, the Board should offset the excess earnings realized by the carrier's domestic routes while operating under a final mail rate.

2. Whether the Board should recognize and apply the actual Federal income tax rate, rather than a 38 percent tax rate, for the purpose of computing the tax allowance in the rates to be established for the Latin American division of C&S.

Since, except as stated above, our findings and conclusions in the Tentative Statement have not been contested as to matters entering into the determination of mail rates for this carrier, resolution of these issues is all that remains necessary for the determination of the fair and reasonable final mail rates.

248 *The Offset of Earnings of the Domestic Routes
Against The "Need" of the Latin American Routes*

During part of the past period involved in this proceeding, namely, 1948-1950, the domestic routes of C&S were operated under final mail rates which yielded the carrier an average rate of return on investment estimated at 12.5 percent. When fixing these mail rates, the Board had estimated a rate of return of 7.4 percent for the carrier from its domestic operations. In undertaking the issuance of a Statement of Tentative Findings and Conclusions for mail rates for C&S' international routes in this case we gave careful consideration to the possible offset of such excess earnings against the "need" resulting from the carrier's international operations. We decided, however, for reasons of economic policy, that no offset should be made.¹ The Postmaster General has objected to this finding, arguing that the "all other revenue" language of section 406(b) of the Act requires that the Board offset the excess earnings from domestic operations under the final rate against the "need" resulting from international operations in establishing rates applicable to both the past and future operations of the international routes. The carrier and the Bureau Counsel maintain that there is no duty of offset, and urge that none be made. In fact, Bureau Counsel questions the Board's power to offset earnings of one segment of an air carrier's operations under an unchallenged final mail rate against the "need" incurred on a different part.

249 After careful consideration of the various contentions of the parties, we conclude that we are not required to make the offset urged by the Postmaster General. Subsequent to the issuance of our Tentative Statement in this proceeding we had occasion in the *Western Air Lines, Inc.-Inland Air Lines, Inc., Mail Rates Case*,² to express an

¹ At the same time we pointed out that we had the power to institute proceedings to reduce rates and that we were having the staff make studies of C&S' earnings to determine whether such proceedings should be instituted. As a result of these studies, we issued an order on October 1, 1951 (Order Serial No. E-5747), reopening the current final mail rates for the domestic operations of C&S and six other domestic trunkline operators.

² Order Serial No. E-5467, adopted June 26, 1951.

opinion on the obligation imposed on us by the Act to consider "other revenue" for the purpose of reducing need in final mail rate proceedings. We there concluded that while we are required to take into consideration the need of a carrier for mail compensation together with "all other revenue", we believe that we are not required by section 406(b) to reduce the carrier's mail pay with any part of such other revenue if there are sound reasons for not doing so as a matter of economic policy. Reappraising that opinion in the light of this case, we consider that the same principle is applicable here in view of the policy considerations which we discuss below.

If an offset policy were adopted, the almost invariable result would be that, as in the instant case, the profits from a carrier's domestic operation would be used to sustain any international operations it might have. Recognizing this likelihood, we hesitate to burden the more robust segment of the industry with the obligations of the economically weaker part. For if the domestic air transport system can be kept financially sound, the public must ultimately benefit, putting aside any consideration of the obvious advantage of reduced rates of mail compensation. Thus, we anticipate that if the carriers' earning position continues strong, reductions in the domestic fare level will be possible, thereby giving impetus to the further development of the
 250 industry. In addition, with improved earnings, the domestic operators should be able to benefit the public and themselves with more modern aircraft, and with improved methods affording safer and more efficient operations. We cannot escape the thought that if we allow international operations to be carried on the back of domestic operations, we shall be subjecting the latter to an unjustifiable strain. Many of the domestic operators are well along the road to self-sufficiency. It is our duty to speed them on their way, not thwart them.

It also appears desirable to maintain the comparative status between those domestic operators which have foreign routes as against those which do not have foreign routes.

Since carriers fall into fairly well-defined classes, the Board is enabled to fix uniform domestic mail rates for groups of carriers provided, of course, that their comparative status is preserved by excluding consideration of any international operations. A carrier operating under a class rate has every incentive to operate efficiently because it may retain any profits it earns in excess of the estimated return to be afforded by the uniform rate. It is also administratively desirable to preserve a comparative status between carriers because the Board has been able to analyze the operations of each carrier within a class in the light of the results achieved by others within the same class. The comparison technique of rate-making has proved to be the most satisfactory and practicable available to the Board. If we were required to fix rates for both domestic and international operations at the same time, it would be difficult, if not impossible, to find a suitable basis for a comparison technique of analysis.

251 In view of the foregoing, we find that the earnings from C&S' domestic routes should not be used to offset the "need" resulting from the carrier's international routes. This conclusion stems from considerations of economic policy; we are not deciding the question of our legal power to make such an offset.

The Allowance for Federal Income Taxes

The Postmaster General objects that it is not proper to recognize in the mail rate to be paid by the Government any actual corporate tax rate increase in excess of 38 percent because such an allowance would defeat the basic purposes of the tax increases, namely, to raise the public funds necessary to meet the national defense emergency and to safeguard against further inflationary tendencies. He adds that the carrier, like other citizens, should bear its share of the increased tax burden.

Although the parties have agreed that the tax return technique which we adopted in the *Western-Inland Mail Rates Case* should be employed in this proceeding, the

Postmaster General, who strongly favored such a technique, now wishes to depart from it to the extent that he proposes to recognize only a 38 percent tax rate instead of the higher actual rate of 42 percent during 1950 and 47 percent thereafter. Bureau Counsel and the carrier oppose this contention. Under the Postmaster General's theory a tax allowance would be derived which falls short of meeting the carrier's actual tax liability as reflected on the face of the return. In view of the nature of the tax return technique of making provision for taxes, we cannot accept the Postmaster General's argument.

It is well established that in fixing the rate to be allowed a public utility for a proper income, the Federal income tax must be provided for as an operating charge.

252 The courts have followed this principle and the Board itself has followed it in all of its mail rate decisions. During the period when Federal income tax rates on corporations were gradually raised from 19 percent in 1938 to the 38 percent level prior to 1950, the Board and other regulatory agencies recognized these increases as proper operating charges in determining what rates would constitute a fair return on investment.³

As we indicated in the *Western-Inland Mail Rates Case* the purpose of the tax allowance is to afford the carrier an opportunity to realize the full rate of return which the Board has determined it should properly be granted to meet its statutory needs. Thus, we have determined in this case that the carrier is entitled to a rate of return of 7 percent for the past period and 10 percent for the future period. The Postmaster General has not demonstrated that the rates of return prescribed for C&S and carriers of its class are excessive or unreasonable under current conditions. Yet, if the carrier is taxed at the 47 percent rate, but the allowance for taxes is based on a hypothetical 38 percent rate, as the Postmaster General suggests, C&S will have after taxes a rate of return on investment of

³ Of course, our discussion of the proper Federal income tax allowance does not cover the question of excess profits taxes since they are not in issue here.

only 5.9 percent for past periods and 8.5 percent for future periods rather than the returns which the Board has found to be reasonable.

Finally, another basic flaw in the Postmaster General's argument is that he assumes an increase in corporate taxes will automatically reduce the net income of unregulated enterprises, and, therefore, that it would be unjust to permit air carriers an exemption from this general re-

duction in corporate net income after taxes. However, there is nothing in the recently enacted price control or tax legislation which indicates a congressional intention to reduce the profits earned either by ordinary corporations or public utilities to a level which falls below a fair and reasonable return.

CONCLUSION

In view of the foregoing, we find that the objections of the Postmaster General to the Statement of Tentative Findings and Conclusions (Order Serial No. E-5385) issued in this proceeding should be denied. However, an adjustment must be made in the rate of mail compensation for the past period. This arises from the fact that the parties have stipulated that the allowance for Federal income taxes of \$130,000 made in the Tentative Statement should be increased to \$147,000. This change results from the application of the tax return technique of determining the proper allowance for Federal income taxes instead of the "hybrid" method which was used by the Board in the Tentative Statement but which has been abandoned since that time.⁴ Accordingly, we reaffirm and hereby adopt our findings in the Statement of Tentative Findings and Conclusions, except with respect to the allowance for Federal income taxes in the past rate period and the issue of offset discussed above.

Therefore, we now find that compensation for the transportation of mail over its international routes

⁴ Adoption of the tax return technique was first announced by the Board in *Western Air Lines, Inc.-Inland Air Lines, Inc., Mail Rates*, Order Serial No. E-5467, adopted June 26, 1951.

by C&S for the period November 1, 1946-December 15, 1950, inclusive, should be fixed at \$3,662,000.

An appropriate order will be entered.

Nyrop, Chairman, Ryan, Lee, Adams, and Gurney, Members of the Board, concurred in the above opinion.

255

Orders

Serial Number E-5793

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board at its office in Washington, D. C., on the 18th day of October, 1951.

Docket No. 2564

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.

over its Latin American Route.

Order Fixing and Determining the Fair and Reasonable Final Rates of Compensation for the Transportation of Mail by Aircraft

A public hearing having been held in the above-entitled proceeding, and the Board, upon consideration of the record, having issued its opinion containing its findings, conclusions, and decision, which is attached hereto and made a part hereof;

IT IS ORDERED, That the fair and reasonable rates of compensation to be paid to Chicago and Southern Air Lines, Inc., for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith between the points on its Latin American routes between which the carrier is presently or hereafter may be authorized to transport mail by its certificates of convenience and necessity are as follows:

1. For the period November 1, 1946-December 15, 1950, inclusive, the sum of \$3,662,000.¹
2. For the period on and after December 16, 1950:

For each calendar month an effective rate per designated mile flown obtained by dividing by the designated miles flown during the month the product of 3.41 cents times the lower of 4,529,000 or the standard available seat-miles flown in scheduled passenger service during the month. For the period from December 16, 1950, to December 31, 1950, the mail rate shall be derived by dividing by the designated miles flown therein the product of 3.41 cents times the lower of 2,264,500 or the standard available seat-miles flown in scheduled passenger service during the period.

256 The available seat miles flown in scheduled passenger service during the month shall be computed by multiplying the scheduled mileage flown in passenger service during the month with each aircraft type by the standard available seats for that type as specified below:

Aircraft Type	Seats
DC-3	21
DC-4	44
Constellation	52

The aforesaid rates per airplane mile shall be applied to, and the designated mileage flown shall be computed on, the direct airport-to-airport mileage between points served for the carriage of mail on each trip flown on a schedule designated or ordered to be established by the Postmaster General for the carriage of mail, and the scheduled mileage flown shall be computed on the direct airport-to-airport mileage between points actually served on each trip flown in scheduled passenger service, including all trips operated as extra sections thereto.

The compensation provided above shall be inclusive of, and not in addition to, the mail compensation received by the carrier for the transportation of mail on and after November 1, 1946, over its Latin American route.

¹ This amount is equivalent to a rate of 78.87 cents per recognized revenue/plane mile flown in scheduled service over the international system.

IT IS FURTHER ORDERED, That the aforesaid order fixing fair and reasonable rates shall be effective as of this date, all parties to the above-entitled proceeding having already waived all procedural requirements subsequent to hearing short of a final decision of the Board fixing rates herein.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN

M. C. MULLIGAN

Secretary

(Seal)

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BEFORE THE
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Docket No. 2564

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.

over its Latin American Route.

Petition to Reconsider

TO THE CIVIL AERONAUTICS BOARD:

The Postmaster General, pursuant to Section 302.11 of the Board's Rules of Practice, hereby petitions the Board to reconsider the ruling for mail rate-making purposes which fails to take into account the excess earnings realized by the carrier from its domestic operations when fixing and determining the true subsidy need of the carrier, Chicago and Southern, during the same period of time involved for the Latin American operation of C. & S. The ruling is set forth in the Board's Opinion and Order E-5793, of October 18, 1951, in the above-entitled rate proceeding. The said ruling is challenged herein on the grounds that:

I

The mail rate section (406(b)) of the Civil Aeronautics Act requires the Board to apply the excess earnings of the domestic system—as “other revenue”—when determining the true need of the carrier as a whole for subsidy mail compensation.

II

The Board has failed to consider the Postmaster General's contention that C. & S. has no “need” for additional compensation for its Latin American operations to the extent that C. & S. has received excess earnings from its domestic operations which meets the need requirements of the Latin American operations for the same period of time.

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III

Excess subsidy should never be deemed to be needed in order to maintain an air transport system on a sound financial basis.

IV

The Board's reason—to enable the Board to provide a uniform class mail rate for groups of carriers—used as a foundation for the rule in question is not supported by actual facts and practices.

• • • • •

UNITED STATES OF AMERICA
CIVIL AERONAUTICS BOARD
WASHINGTON, D. C.

Adopted by the Civil Aeronautics Board
at its office in Washington, D. C. on
the 18th day of January, 1952.

Docket No. 2564

In the matter of the compensation for the transportation
of mail by aircraft, the facilities used and useful there-
for, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.
over its Latin American Route.

Order Denying Petition for Reconsideration

The Board having issued on October 18, 1951, an opinion and order¹ fixing final mail rates for both past and future periods for the Latin American operations of Chicago and Southern Air Lines, Inc.;

The Postmaster General of the United States having filed on November 19, 1951, a petition for reconsideration of this opinion and order only insofar as the Board decided not to offset the excess earnings realized by the carrier's domestic operations against the "need" on its Latin American operations, and the carrier and Bureau Counsel having filed their respective answers to the petition for reconsideration in support of the Board's decision;

The Board, upon consideration of the petition of the Postmaster General, finding that it contains no matter not previously considered by the Board herein, and that the matters set forth therein do not warrant the granting of the relief requested;

¹ Order Serial No. E-5793.

IT IS ORDERED, That the petition for reconsideration of the Postmaster General be, and it hereby is, denied.

By the Civil Aeronautics Board:

/s/ M. C. MULLIGAN
M. C. Mulligan
Secretary

(SEAL)

183-A

BEFORE THE
CIVIL AERONAUTICS BOARD

Docket No. 2564

In the matter of the compensation for the transportation of mail by aircraft, the facilities used and useful therefor, and the services connected therewith, of

CHICAGO AND SOUTHERN AIR LINES, INC.

over its Latin American Route.

[Excerpts From] Stipulation and Waiver Respecting Answer of the Postmaster General

WHEREAS the Board has heretofore issued in the above-entitled proceeding an Order directing the parties to show cause why the Board should not adopt the proposed rates set forth in the Statement of Tentative Findings and Conclusions, accompanying the said Order Serial Number E-5385, adopted May 18, 1951, in Docket No. 2564;

AND WHEREAS the Post Office Department having filed a notice of objections to said Order, and its accompanying Statement of Tentative Findings and Conclusions, and an Answer, dated June 14, 1951 filed pursuant to Section 302.13(c) of the Procedural Regulations of the Board, which said Answer objected to the Board's method of computing Federal income taxes for the past and future rate-making periods involved, and also to the Board's refusal to take into account the excess earnings of the domestic division when considering the needs of Chicago and Southern's international division;

183-B AND WHEREAS all of the parties desire to expedite the final disposition of this rate proceeding they have decided to waive certain procedural steps and enter into a stipulation concerning the factual issues raised by the said Answer, leaving the legal and policy issues thereby presented for determination by the Board;

Now THEREFORE this stipulation entered into this 31st day of July, 1951, between the parties in the above-entitled proceeding witnesses that Chicago and Southern Air Lines, Inc., the Post Office Department and Bureau Counsel, do agree and consent, as follows:

* * * * *

183-C (5) That the total earnings, in excess of whatever rate of return on recognized investment shall be adopted as a standard for this purpose by the Board, realized by the domestic division of Chicago and Southern Air Lines, Inc. during the past period commencing January 1, 1948, and extending through December 15, 1950 were as shown in the computations made by the staff, which are attached hereto as Appendix II, and that such computations be made a part of this Stipulation;

* * * * *

183-I

Appendix II

CHICAGO AND SOUTHERN AIR LINES, INC.

Computation of Earnings from Domestic Operations to be Offset in
the Mail Rate for the International Division
Years 1948-1950
(in thousands)

	1948	1949	1950	Total
Domestic Operating Net Profit:				
As reported	\$ 446	\$ 471	\$ 470	\$1,387
Adjustments (see page 2)	69	115	31	215
Total	<u>\$ 515</u>	<u>\$ 586</u>	<u>\$ 501</u>	<u>\$1,602</u>
Investment	\$4,150	\$4,035	\$4,617	\$4,267
Rate of Return	12.41%	14.52%	10.85%	12.51%
Earnings Above:				
8 percent	\$ 183	\$ 263	\$ 132	\$ 578
10 percent	100	182	39	321

183-J

CHICAGO AND SOUTHERN AIR LINES, INC.

Computation of Net Profit Adjustments
Years 1948-1950
(in thousands)

	1948	1949	1950	Total
<i>Expense Additions</i>				
Adjustment of DC-3 depreciation to reflect change in service life	\$125	\$ 63	\$ —	\$188
DC-4 equipment integration costs	36	26	37	99
Accounting change in allocation of joint expenses due to excess capacity disallowance in international operations:				
Depreciation	—	—	21	21
Ground Operations	—	—	8	8
Ground and indirect maintenance	—	—	10	10
General and administrative exp.	—	—	23	23
Total	<u>\$161</u>	<u>\$ 89</u>	<u>\$ 99</u>	<u>\$349</u>
<i>Expense Deductions</i>				
Adjustment of DC-4 depreciation to reflect changes in service life	\$148	\$204	\$103	\$455
Profit on sale of DC-4 aircraft allocated to domestic system	—	—	27	27
DC-3 depreciation charged by carrier ¹	82	—	—	82
Total	<u>\$230</u>	<u>\$204</u>	<u>\$130</u>	<u>\$564</u>
Total Adjustment to Reported Net Profit	<u>\$ 69</u>	<u>\$115</u>	<u>\$ 31</u>	<u>\$215</u>

¹ After domestic rate order of July 1, 1948 C&S changed service life of DC-3 aircraft from common retirement date of 6-30-47 to 12-31-48.

**In the United States Court of Appeals
for the District of Columbia Circuit**

JESSE M. DONALDSON, Postmaster General
of the United States, and

THE UNITED STATES OF AMERICA on behalf of the
Postmaster General, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

On Petition for Review of Order of the Civil Aeronautics Board

BRIEF FOR PETITIONERS

United States Court of Appeals
For the
District of Columbia Circuit

FILED JUL 9 1952

Joseph W. Stewart
CLERK

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DANIEL M. FRIEDMAN,
Special Assistant to the
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Washington 25, D. C.

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ARNE C. WIPREUD,
Associate Solicitor.

FREDERICK E. BATRUS,
Assistant Solicitor.

EUGENE J. BRAHM,
Chief, Air Mail Section.
Post Office Department,
Washington 25, D. C.

QUESTIONS PRESENTED

Chicago and Southern Air Lines ("C & S") conducts both domestic and Latin American operations. In 1948 the Civil Aeronautics Board fixed a final prospective subsidy mail rate for C & S's domestic operations which it estimated would yield the carrier a net return after taxes of 7.4% on that portion of its property allocable to domestic operations. Actual operations under that rate, however, resulted in an average return on domestic operations for the years 1948 through 1950 of 12.51%, or \$654,000 more than a 7.4% rate of return would have produced. In 1951 the Board, in fixing subsidy mail pay for those years for C & S's international operations, refused to offset the excess profit of \$654,000 attributable to domestic flights. Section 406(b) of the Civil Aeronautics Act directs the Board, in fixing mail pay, to "take into consideration, among other factors, * * * the need of each such air carrier for compensation for the transportation of mail sufficient * * * together with all other revenue of the air carrier * * *" to enable the carrier to "maintain and continue the development" of a national air transportation system. The questions presented are:

1. Whether the Board is empowered under Section 406 (b) of the Act to award a subsidy in the form of "need mail pay" which is greater than the carrier's "need."

2. Whether Section 406(b) authorizes the Board to award "need" mail pay on the basis of the needs of particular operating divisions of a carrier without regard to the need of the carrier as a whole.

3. Whether Section 406(b) requires the Board, in determining a carrier's "need" for subsidy, to offset *all* other revenue of the carrier.

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In the United States Court of Appeals for the District of Columbia Circuit

No. 11,351

JESSE M. DONALDSON, Postmaster General
of the United States, and

THE UNITED STATES OF AMERICA on behalf of the
Postmaster General, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

On Petition for Review of Order of the Civil Aeronautics Board

BRIEF FOR PETITIONERS

JURISDICTIONAL STATEMENT

The jurisdiction of this Court is invoked under Section 1006 of the Civil Aeronautics Act of 1938, 52 Stat. 1024, 49 U.S.C. 646. The final order of the Civil Aeronautics Board, fixing mail pay for Chicago and Southern Air Lines for its Latin American operations, was entered on October 18, 1951 (J. A. 58).¹ The petition to review that order was filed on March 18, 1952, within 60 days after the Board denied the Postmaster General's petition for reconsideration on January 18, 1952 (J. A. 62.)² Section 1006, *supra*;

¹ Throughout this brief, the joint appendix will be cited as "J. A.".

² The Postmaster General is required to pay air carriers for transporting air mail, out of funds appropriated by Congress for that purpose, at the rates fixed by the Board. Section 406(a). He participates in all air mail pay proceedings before the Board, and serves as the protector of the public interest in such proceedings. *Seaboard & Western Air Lines v. Civil Aeronautics Board*, 86 U.S. App. D.C. 64, 67-68, 181 F. 2d 515, 518-519, certiorari denied 339 U.S. 963. The Postmaster General thus has a substantial interest in the order under review within the meaning of Section 1006 of the Act. Cf. *Far East Conference v. United States*, 342 U.S. 570, 576.

Braniff Airways v. Civil Aeronautics Board, 79 U. S. App. D. C. 341, 147 F. 2d 152. The opinions of the Civil Aeronautics Board have not been published in bound form; they are set forth in the joint appendix, pages 6-60.

STATEMENT OF THE CASE

Chicago and Southern Air Lines ("C & S") is a certificated air carrier conducting both domestic and Latin American operations.³ The petition for review challenges an order of the Civil Aeronautics Board which fixed "need" (i.e. subsidy) mail pay covering the carrier's Latin American routes. It is petitioners' contention that the Board violated the plain terms of Section 406(b) of the Civil Aeronautics Act by failing to offset C & S's "excess" profits on its domestic operations in determining the carrier's subsidy "need" on its foreign routes. The underlying facts are undisputed.

Separate proceedings were conducted by the Board to fix C & S's domestic and foreign mail rates. Final domestic rates were fixed in July, 1948. *Chicago and Southern Airlines, Mail Rates*, 9 C.A.B. 786. They included a past rate for the period January 1, 1946, through December 31, 1947 (not involved in this case), and a prospective rate for the period commencing January 1, 1948.⁴ The Board estimated that the future rate would yield C & S a net return after taxes of 7.4% on that part of its investment allocable to domestic operations. Actual operations under the rate, however, resulted in an average return on domestic operations for the years 1948 through 1950 of 12.51%.⁵ This was \$654,000 more than a 7.4% rate of return would have produced.

³ C & S's domestic routes are between Chicago/Detroit/Kansas City and Houston/New Orleans. See 9 C.A.B. 786, 789-90. The carrier's international routes are between Houston/New Orleans and various points in the Caribbean and Caracas, Venezuela (J. A. 7).

⁴ Both the domestic and the international rates were fixed upon the basis of an allocation of the carrier's expenses and investments common to both domestic and foreign services. 9 C.A.B. at 803-804, 809, 812-813; J.A. 17-18, 21, 28-29).

⁵ J. A. 53. Figures relating to C & S's domestic rate of return during those years are contained in a stipulation entered into during the Board proceedings in the instant case (J. A. 63).

On October 18, 1951, the Board issued its opinion and order fixing final subsidy mail pay rates for C & S's Latin American operations (J.A. 51).⁶ Rates were fixed retroactively for the period from November 1, 1946, to December 15, 1950, and prospectively from December 16, 1950 (J.A. 59).⁷ The rates were fixed to give the carrier a rate of return after taxes on its property allocable to foreign operations of 7% for the past period (J. A. 23), and 10% for the future (J. A. 30).

In fixing the rates, both retroactively and prospectively, the Board refused to offset C & S's "excess" profits on its domestic routes against the carrier's "need" resulting from its international operations (J. A. 53-55).^{7a} The Board reaffirmed and applied the principle it had previously enunciated in the contemporaneous *Western Airlines* case⁸—that Section 406(b) of the Civil Aeronautics

⁶ C & S was certificated on its Latin American routes on May 17, 1946. *Latin American Air Service*, 6 C.A.B. 857, 927 (1946). Service over these routes was inaugurated November 1, 1946 (J.A. 8). A petition to fix mail rates for these routes was filed by C & S in October, 1946 (*ibid.*) On May 18, 1951, the Board issued a statement of tentative findings and conclusions proposing final rates for C & S's foreign operations (J. A. 6).

The tentative findings concluded that the carrier's "excess" domestic earnings should not be offset "against the need which would otherwise be found to exist in relation to C & S's international operations" because "policy considerations" rendered such an offset "inappropriate" (J. A. 19). The Board stated that the airline industry could best achieve economic self-sufficiency, from the mail rate standpoint, by placing carriers on final future rates as soon as possible; that determination of a final future rate is an "exacting" task where the carrier operates only in the domestic or in the foreign field; and that unless final future domestic rates could be fixed without simultaneously determining international rates, "it may often prove to be impossible to fix any permanent rate for the carrier for an extended period of time" (J. A. 20).

The Postmaster General filed objections to the proposed rates on the ground, *inter alia*, that the Board improperly refused to offset the "excess" domestic earnings (J. A. 52).

⁷ Temporary foreign mail pay rates had been fixed by the Board in March, 1947 (7 C.A.B. 985), and May, 1948 (9 C.A.B. 924).

^{7a} The Board's refusal to offset the excess profits for the past period resulted in the carrier receiving an additional \$654,000 in subsidy mail pay (cf. J. A. 65).

The amount of such excess for future periods has not been calculated. However, petitioners' challenge of the future rates relates only to the period December 16, 1950, to September 30, 1951. Effective October 1, 1951, C & S's domestic rates were substantially reduced. *Chicago and Southern Air Lines, Domestic Operations, Mail Rates*, Docket No. 5144, Order No. E-5956, December 19, 1951. The Board order instituting those proceedings recited that the then existing domestic rates appeared "to have become or will be excessive." *Ibid.*, Order E-5747, Oct. 1, 1951.

⁸ *Inland Air Lines-Western Air Lines, Mail Rates*, Docket No. 2870, et al., Order No. E-5467, June 26, 1951, petition to review pending *sub nom. Donaldson v. Civil Aeronautics Board*, C.A.D.C., No 11,259.

Act does not require it to reduce the carrier's mail pay by offsetting any part of the carrier's other revenue "if there are sound reasons for not doing so as a matter of economic policy" (J. A. 54). The Board stated that if profits from domestic operations were used to "sustain" international flights, the "more robust" domestic segment of the industry would be burdened with the obligations of the "economically weaker" international segment. By maintaining the domestic segment in a "financially sound" position, the Board continued, the public will benefit through lower fares, reduced mail compensation, more modern aircraft and improved operating methods (*ibid.*). The Board further stated that it was "desirable" to maintain the "comparative status" between domestic operators with and those without foreign routes, in order to permit the Board to continue using the comparison technique for fixing class rates for domestic carriers (J. A. 54-55).⁹

A petition for reconsideration filed by the Postmaster General, again challenging the propriety of the Board's failure to offset the "excess" domestic earnings (J. A. 60-61), was denied by the Board without opinion (J. A. 62).

STATUTE INVOLVED

The Civil Aeronautics Act of 1938, 52 Stat. 977, as amended, 49 U. S. C. 401 *et seq.*, provides in pertinent part as follows:

Section 406(a) The [Board] * * * is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, * * * and the rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft. [49 U. S. C. 486(a).]

⁹ The Board stated that its decision not to make the offset stemmed from "considerations of economic policy," and that it was not deciding the question, raised by Board counsel (J. A. 53), of its power to make the offset (J. A. 55).

Section 406(b) In fixing and determining fair and reasonable rates of compensation under this section, the [Board] * * *, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the [Board] * * * shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense. [49 U. S. C. 486(b).]

STATEMENT OF POINTS

The Civil Aeronautics Board erred:

1. In failing to apply the \$654,000 "excess" profits from C & S's domestic operations for 1948 through 1950 in determining the carrier's need for subsidy mail pay on its Latin American routes during those years.
2. In fixing need mail pay for C & S's Latin American operations without regard to the need of the carrier as a whole.
3. In holding that Section 406(b) of the Civil Aeronautics Act authorizes it to exclude, because of policy considerations, any portion of a carrier's "other revenue" in determining a carrier's subsidy need.

SUMMARY OF ARGUMENT

I

Section 406(b) of the Civil Aeronautics Act, which formulates the standards to be followed by the Civil Aeronautics Board in fixing "fair and reasonable" mail pay rates, distinguishes between compensation for carrying the mail, and subsidy payments to insure the development of a national system of air transportation in accordance with the statutory objectives. The Board has recognized this distinction; it fixes mail pay on either a "service" (i.e., compensatory) or on a "need" rate. The "need" rate is an acknowledged subsidy. In fixing that rate, however, the Board cannot award subsidy in an amount in excess of what the carrier "needs," as that term is defined in Section 406(b). The Act does not authorize the Board to award a subsidy which gives the carrier an over-all rate of return greater than the aggregate of the needs of its individual divisions.

II.

The need referred to in Section 406(b) is the need of the carrier as a whole, and not the need of particular operating divisions. Prior to the instant case, the Board has consistently recognized that principle. The decision under review departs from this construction. For, by refusing to offset C & S's "excess" profits on its domestic routes, the Board has determined the carrier's need for subsidy on its international operations as if the latter were those of a separate carrier. The Board's power administratively to fix rates separately for different operating divisions of a carrier does not override the statutory limitation that the total subsidy awarded cannot exceed the need of the carrier as a whole.

III

Section 406(b) defines a carrier's need as the amount required to accomplish the statutory objectives after offsetting "all other revenue" of the carrier. The Act thus

requires that *all*—not some—other revenue be offset in determining a carrier's need, and does not authorize the Board to exclude any part of such other revenue because of policy considerations. A statute providing for subsidization of private enterprise at public expense should be strictly construed. The Board's treatment of the "all other revenue" clause in Section 406(b) could lead to the emasculation of the entire need standard.

ARGUMENT

I

Subsidies in the Form of Mail Pay May Be Granted Only to the Extent of the "Need" of the Carrier

Section 406(a) of the Act directs the Board to fix "fair and reasonable" rates of compensation for the transportation of mail by aircraft. Section 406(b) provides that in determining such rates, the Board "shall take into consideration," *inter alia*,

* * * the need of each such carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense.

The Act thus distinguishes between the carrier's respective needs for compensation sufficient (1) to insure the transportation of mail, and (2) to enable the carrier to aid the development of a national system of air transportation.

The Board has recognized this distinction in fixing mail pay rates. Such rates may be calculated on what the Board describes as a "service" basis or a "need" basis. "Service" payments are intended to provide the carrier with fair compensation for carrying the mail, and sup-

posedly contain no subsidy elements.¹⁰ A "need" rate, on the other hand, bears no relationship to the carrier's services in carrying the mail,¹¹ but is an acknowledged subsidy to maintain the carrier as an efficient going-concern. The "need" rate is fixed by the Board at a level to provide the carrier with sufficient income to (1) meet its entire operating charges, (2) pay its taxes, and (3) earn a fair rate of return on its total invested capital.¹² Since, however, the carrier is required to operate under "honest, economical, and efficient management," the Board disallows excessive or improper expenditures in determining the carrier's need.

"Section 406(b) of the Act * * * requires that mail pay shall be awarded in an amount corresponding to the statutory 'need' for such compensation as a means of maintaining and continuing the development of air transportation in the public interest * * *."¹³ Although need is not the only factor to be considered, it plainly is a mandatory, limiting feature, i.e., the Board cannot award mail pay in an amount in excess of what the carrier needs.

Without the "carefully worded 'need' formula which the Act sets for the Board's guidance in fixing the air mail 'compensation' "¹⁴ the Board would be left without any major standard to guide it in fulfilling its statutory duty

¹⁰ *Eastern Air Lines, Mail Rates*, 3 C.A.B. 733, 755, 760 (1942). "Service" rate payments are not limited to reimbursement of expenses of carrying the mail, but also include a fair profit to the carrier for rendering the service. *Id.* at 755-756.

¹¹ For example, the Board has allocated "need" payments to particular routes although no mail was carried on them. *Chicago and Southern Air Lines, Mail Rates*, 3 C.A.B. 161, 190 (1941).

¹² *Pioneer Air Lines, Mail Rates*, 8 C.A.B. 175, 187 (1947). The Board generally allows a 7% return for past periods on both domestic and international operations (*Western Air Lines, Mail Rates*, Docket No. 2870, Order No. E-4870, November 27, 1950, mimeographed p. 47; J.A. 23). For future periods, the return generally is 8% for domestic operations (*Chicago and Southern Air Lines, Domestic Operations, Mail Rates*, Docket No. 5144, Order No. E-5869, November 15, 1951) and 10% for foreign operations (J.A. 30).

¹³ *Western Air Lines, Mail Rates*, Docket No. 5148, Order No. E-6295, April 7, 1952, at mimeographed p. 11. Accord: *American Airlines, Mail Rates*, 3 C.A.B. 323, 335-338 (1942); *Pan American Airways, Alaska Mail Rates*, 6 C.A.B. 61, 67 (1944); *Pan American Airways, Latin-American Mail Rates*, 6 C.A.B. 85, 91 (1944); *Pan American Airways, Trans-Pacific Mail Rates*, Docket No. 2147, Order No. E-5882 (November 21, 1951, mimeographed p. 21).

¹⁴ *American Airlines, Mail Rates*, 3 C.A.B. 323, 335 (1942).

of using mail payments as a device for developing air transportation. See Section 406(b); cf. *American Airlines, Mail Rates*, 3 C.A.B. 323, 335. The statutory mandate "shall take into consideration," read in the context of language which carefully formulates the elements to be considered by the Board in determining a carrier's need, cannot be construed as a grant of unlimited discretion to the Board to accept or reject the need criterion as it sees fit. Congress could scarcely have intended that the Board, after determining a carrier's need for revenue in accordance with the statutory standards, might grant a subsidy—described by the Board itself as "need" mail pay—in excess of such need.

The Board's construction of the Act, however, would give a carrier subsidy in excess of its actual need. In the instant case the Board awarded domestic "need" subsidy which it estimated would yield a return after taxes for the years 1948-1950 of 7.4% on property allocable to domestic operations. In fixing foreign subsidy pay, it gave the carrier a 7% rate of return after taxes for those years. Thus the Board in effect found that C & S "needed" a 7.4% return on domestic and a 7% return on foreign operations.

The whole cannot exceed the sum of the parts; the carrier's total need cannot add up to more than the total of the needs of each division. Yet the result reached by the Board in this case had precisely that effect. For, by treating C & S's domestic profits as if the \$654,000 "excess" had not in fact been earned, the Board has awarded subsidy mail pay that gives the carrier an overall return during those years considerably in excess of 7.4%.

Hindsight now indicates that in the period 1948-1950 C & S received a subsidy for its domestic routes substantially in excess of its actual need. The carrier cannot complain if its foreign subsidy is accordingly limited to reflect its total overall need. That need—and no more—is what Section 406(b) entitles it to. Offsetting the excess domestic profits would not deny C & S a fair rate of return on each of its divisions. On the contrary, the carrier would

still be receiving a 7.4% return on its domestic and a 7% return on its international operations—rates that the Board has found to be fair. Under such circumstances, the carrier has no claim to further subsidy.¹⁵ Surely the Act does not contemplate that a carrier is to be given a subsidy which produces an overall rate of return substantially greater than the aggregate of the needs of its individual divisions.

II

The "Need" Referred to in Section 406(b) is the Need of the Carrier as a Whole, and Not the Need of Particular Operating Divisions.

The Board's opinion does not reject the view that "need" is a limiting factor. But it states "that the earnings from C & S' domestic routes should not be used to offset the 'need' resulting from the carrier's international routes" (J. A. 55). The result is to compartmentalize the carrier for mail pay purposes in a manner not authorized by the statute.

Section 406(b) makes it abundantly clear that the "need" referred to is the need of the carrier as a whole, and not the need of particular operating divisions of the carrier. The need clause begins with a reference to the need of "each such air carrier." The "other revenue" clause similarly refers to all other revenue of "the air carrier," and speaks of compensation which, together with such other revenue is sufficient to enable "such air carrier" to carry out the statutory objectives. The Act thus establishes the air carrier—and not particular routes or divisions thereof—as the "primary unit around which the national air transportation system was to be developed through the instrumentality of air mail compensation." *Chicago and Southern Air Lines, Mail Rates*, 3 C.A.B. 161, 190.

Until its decision in the instant case the Board consistently recognized this principle. In the *Chicago and*

¹⁵ Cf. *Dayton Goose Creek Ry. Co. v. United States*, 263 U.S. 456, 481-483; *Northern Pacific Ry. Co. v. North Dakota*, 236 U.S. 585, 604.

Southern case, *supra*, the Board, in deciding that it could award subsidy mail pay covering routes on which no mail was carried, flatly held:

The need [referred to in Section 406(b)] is that of the air carrier as a whole and not that of any particular geographical division of its operations. [*Ibid*].

This view was reasserted in a number of subsequent cases involving mail pay for both domestic and international operations.¹⁶ In the 1944 *Pan American Mail Pay* case, the Board, specifically reaffirming its holding in the *Chicago and Southern* case, held that the carrier had no "need" for subsidy mail pay on its Alaska division because excess earnings from its more profitable divisions greatly exceeded the Alaska division's requirements. *Pan American Airways, Alaska Mail Rates*, 6 C.A.B. 61, 67. This long-standing and hitherto consistent administrative construction of the Act by the agency charged with its administration is entitled to great weight. *United States v. American Trucking Association*, 310 U.S. 534, 549; *Norwegian Nitrogen Products Co. v. United States*, 288 U.S. 294, 315; cf. *Federal Power Commission v. Panhandle Eastern Pipe Line Co.*, 337 U.S. 498, 513.¹⁷

The Board's decision in the instant case departs from this settled administrative construction of the Act. For, by refusing to offset C & S's excess earnings on its domestic routes in determining the carrier's subsidy need on its foreign operations, the Board treats the Latin American routes as wholly isolated from the carrier's other activities. In other words, the Board has viewed C & S's Latin American operation as if it were that of a separate carrier. Such a construction of the Act flies in the face of the specific directive in Section 406(b) that the Board is

¹⁶ *Delta Air Corporation, Mail Rates*, 3 C.A.B. 261, 271 (1942); *Pan American Airways, Latin-American Mail Rates*, 3 C.A.B. 657, 670 (1942); *Eastern Air Lines, Mail Rates*, 3 C.A.B. 733, 739-740 (1942); *Pennsylvania-Central Airlines, Mail Rates*, 4 C.A.B. 22, 28 (1942); cf. *American Airlines, Mail Rates*, 3 C.A.B. 323, 339 (1942); *Transcontinental & Western Air, Mail Rates*, 4 C.A.B. 139, 143 (1943).

¹⁷ In the *Panhandle* case, the Court, in holding that the Commission had no power under the Natural Gas Act to regulate dealings in gas acreage, pointed out that for more than ten years the Commission had never claimed that power.

to determine the need of the "air carrier"—not the need of a particular operating division.

As we demonstrate in point III, *infra*, Section 406(b) requires the Board, in determining a carrier's need, to offset all other revenue of the carrier. If the Board were permitted to award subsidy mail pay to meet the need of particular operating divisions without regard to the carrier's over-all needs, that requirement would be thwarted. For, if the Board could thus segmentize need, consistency would seem to require that such need should be determined by offsetting only such other revenue as was attributable to the particular division concerned.¹⁸ Section 406(b), however, refers to "*all* other revenue of *the* air carrier." If the clear and unambiguous meaning of those words is to be given its normal effect, the word "need" can only mean the need of the carrier as a whole—as the Board has heretofore consistently held.¹⁹

We are not questioning the Board's power administratively to fix rates separately for different operating divisions of a carrier. We do, however, challenge the Board's position that in determining subsidy for a particular division it can ignore the operating results of other divisions during the same period. The power to treat divisions as separate entities for rate-making purposes does not override the statutory limitation that the *total* subsidy awarded cannot exceed the need of the carrier as a whole. By administratively fixing separate rates for different divisions, the Board cannot give the carrier a greater subsidy than it would receive if rates for all divisions were fixed together.²⁰

¹⁸ The result would always redound to the carrier's benefit and the taxpayer's loss, since mail pay would be used to make up deficits on unprofitable operations, and all revenue from particularly profitable operations would go to the carrier. A carrier whose overall position was excellent could demand and receive need mail pay for one unprofitable segment of its operations.

¹⁹ *Supra*, p. 11.

²⁰ The Board's own experience demonstrates that it is administratively feasible to fix separate rates for particular divisions, and still give effect to the overall need limitation. In the *Pan American* mail rate case, *supra*, separate rates were fixed for the carrier's transatlantic, Alaska, Pacific and

III

Section 406(b) Requires the Board, in Determining the Need of the Carrier for Subsidy, to Offset All Other Revenue of the Carrier

In fixing C & S's subsidy for its international routes for the period November 1, 1946, to December 15, 1950, the Board first calculated that the carrier needed \$3,122,000 in mail pay in order to break even on its international operations (J.A. 19). It then determined the carrier's recognized investment for the period to be \$1,360,000 (J.A. 23). In making these calculations, the Board made various adjustments in the carrier's actual operating results to reflect the statutory concept of "honest, economical, and efficient management." The Board allowed the carrier a return of 7% on such recognized investment, or \$393,000 (J.A. 23). To this was added \$147,000 covering Federal income taxes (J.A. 57). The total mail pay thus computed was \$3,662,000 (J.A. 58).

The Board's refusal to offset the carrier's "excess" profits on its domestic routes (\$654,000) was made in the course of calculating the carrier's break-even point. In determining not to offset these excess revenues, the Board did not hold that C & S "needed" the additional \$654,000. Instead, it merely concluded that such excess profits—admittedly "other revenue"—"should not be used to offset the 'need' resulting from the carrier's international routes" (J.A. 55). This conclusion was grounded on the Board's view that although it is required under Section 406(b) to take all other revenue into consideration in determining the need for mail pay, it may nonetheless refrain, in its discretion, from reducing "the carrier's mail pay with any part of such other revenue if there are sound

Latin American divisions. 6 C.A.B. 59, 61, 83, 85. The Board calculated the "need" of the Alaska and Pacific divisions in terms of the amount needed over and above compensatory mail pay. However, the need of those two divisions was met by offsetting the "excess" earnings from other divisions, and the carrier was not given any need payments on these divisions. 6 C.A.B. 65-69, 78, 89.

reasons for not doing so as a matter of economic policy" (J.A. 54).²¹

We submit that this construction of Section 406(b) by the Board is unwarranted. The intent of Congress reflected in that Section is that a carrier is to receive only such mail pay as it "needs," and that such "need" is to be determined by offsetting *all* its other revenue. Section 406(b) defines the need for subsidy as an amount which is sufficient "together with all other revenue of the air carrier," to enable the carrier to meet the statutory objectives. In other words, the Board is directed in fixing a need rate to award mail pay in an amount which, when added to all the carrier's other revenue, will provide it with funds necessary to carry out the national air transportation policy. Cf. *Pan American Airways v. Civil Aeronautics Board*, 84 U. S. App. D. C. 96, 97, 171 F. 2d 139, 140.²²

There is nothing in the Act to support the Board's view that it may disregard a portion of such other revenue because of economic policy considerations. The term "all other revenue" in the Act does not mean "all or some part of other revenue." The extent of the carrier's need—

²¹ The Board stated at another point in its opinion (J.A. 55) that it was not deciding whether it had the power to make the offset. We submit that it plainly had the power and the duty to do so.

It should be noted that there is no issue here of the Board's power retroactively to reduce final future rates, as was the situation in *Transcontinental and Western Air, Inc. v. Civil Aeronautics Board*, 336 U.S. 601. In the *Transcontinental and Western* case, the Court held that the Board had no power to fix new rates retroactively for a period during which a final rate previously established was in effect and unchallenged by the initiation of a mail rate proceeding. In the instant case, however, there is no question of retroactively reducing C & S's domestic mail pay previously received under a final rate. C & S fully retains all payments had under that rate. The sole question here is whether the Board was empowered to treat excess profits under such rate as non-existent in determining the carrier's subsidy need on its foreign routes. Certainly C & S cannot claim, by virtue of the *Transcontinental and Western* case or otherwise, any right to have such profits disregarded by the Board when subsidy rates for another segment of its operation are fixed. As shown in Points I and II, *supra*, the Board cannot award mail pay subsidy in excess of the need of the carrier as a whole.

²² This Court there stated: "It has developed in some cases that the carrier had no need for mail pay in addition to reasonable compensation for services rendered; but in other cases there was such need, because *all the other revenue* was not sufficient to enable the carrier to meet the objectives of the statute" (emphasis added). And see *Seaboard & Western Airlines v. Civil Aeronautics Board*, 86 U.S. App. D.C. 64, 68, 181 F. 2d 515, 519, certiorari denied 339 U.S. 963.

and we reemphasize that it is the need of the carrier as a whole²³—is wholly unaffected by the source of the other revenue which the Act requires to be offset.

If a statute provided that in fixing the rates of a public utility a regulatory Commission was to take into account all of the utility's plant and property dedicated to the public service, it could hardly be suggested that the agency might "consider" a particular facility and determine that it was so dedicated, but nevertheless elect to exclude it from the rate base. No more can the Board determine that certain income constitutes other revenue, and then "consider" such other revenue in a manner which effectively eliminates it from the final computation of the carrier's need for subsidy.

The requirement of the Civil Aeronautics Act that "all other revenue" is to be offset in determining a carrier's subsidy need reflects an important public policy. Clearly, the carrier does not "need" subsidy if its "other revenue" is sufficient to enable it "to maintain and continue the development of air transportation." To whatever extent the carrier has sufficient "other revenue" to enable it to meet that objective in part, its "need" for subsidy is *pro tanto* diminished. Congress, which recently has shown great concern for the huge subsidies the airlines have received from the public treasury,²⁴ clearly manifested an intent to keep subsidies to a minimum when it adopted the strict "need" standard of Section 406(b).

A statute providing for government subsidy of private enterprise should be construed so as to give effect to the limits prescribed by Congress, which presumably were fixed to safeguard against unwarranted payment of public funds. The Supreme Court has repeatedly pointed out

²³ See *supra*, pp. 10-12.

²⁴ Separation of Air-Mail Pay From Subsidy, Committee Print, May 5, 1950; S. Rep. No. 629, 82d Cong. 1st Sess. (1951).

The Board has estimated that \$270,000,000 of the \$457,000,000 mail pay received by domestic carriers from the passage of the Act in 1938 to June 30, 1951, or almost 60%, represents subsidy. Civil Aeronautics Board, Administrative Separation of Subsidy from Total Mail Payments to Domestic Air Carriers, September 1951, p. 5.

that statutory grants of public property to private individuals are to be strictly construed.²⁵

The Board's treatment of the "all other revenue" clause in Section 406(b) could lead to emasculation of the entire need standard. The same type of "economic policy considerations"²⁶ relied upon by the Board to justify fixing

²⁵ *Slidell v. Grandjean*, 111 U. S. 412, 437; *Central Transportation Co. v. Pullman's Palace Car Co.*, 139 U. S. 24, 49; *Northern Pacific Railway Company v. Soderberg*, 188 U. S. 526, 534; *Northern Pacific Railway Co. v. United States*, 330 U. S. 248, 257.

The Comptroller General recently held that the Federal Airport Act, 60 Stat. 170, 49 U.S.C. 1101 *et seq.*, which authorizes the Civil Aeronautics Administrator to grant federal funds for "airport development," does not empower the Administrator to grant funds to build a civic auditorium and adapt a fire prevention reservoir as a swimming pool at a local airport, even though such facilities would "indirectly promote aviation" by centering community interest in the airport. Comp. Gen. Dec. B-108691, June 4, 1952, 20 Law Week 2600 (June 17, 1952).

²⁶ Since we contend that Section 406(b) requires the Board to offset all of the carrier's other revenue in determining its subsidy need, we deem such "economic policy considerations" irrelevant in fixing subsidy mail pay. We note in passing, however, that if such considerations were material, the ones relied upon by the Board in this case plainly would not justify refusal to make the offset.

The Board's final opinion relies upon two principal economic factors. First, it is suggested that the "more robust" domestic segment of the industry should not be burdened with the obligations of the "economically weaker" international segment (J.A. 54). There are several answers to this. Although this consideration might justify a higher rate of return for international than for domestic operations—as the Board in fact provides—it cannot justify giving a carrier a subsidy in excess of its need. Nor is it clear how the domestic segment of the industry would be prejudiced by application of "excess" profits against a carrier's need on its foreign routes. While this rationale might justify preservation of a carrier's domestic earnings up to a "fair and reasonable" level, it cannot be applied to excess earnings realized through subsidy pay from the public treasury. A carrier on a need rate cannot complain if excess earnings are used to meet its requirements on other segments of its system. If this carrier were not receiving subsidy mail pay, the normal course of business would require its profitable routes to absorb operating losses on less profitable segments. It should not be in any better position by virtue of the fact that its risks of loss are minimized by subsidy payments from the public treasury.

It must be borne in mind that C & S had "excess" profits for 1948-1950 only by virtue of the substantial subsidy it received for those years. The estimated amount of the carrier's domestic subsidy during those years—roughly \$4,500,000—is set forth in Appendix A.

The second factor relied on by the Board is the desirability of maintaining the comparative status between domestic carriers which have foreign routes and those which do not. The Board suggests that elimination of such status would handicap it in fixing class rates, although it does not indicate how

independent rates for domestic and international operations, without regard to each other, might also be said to justify awarding domestic need mail pay for particular divisions or even routes. Carried to its logical conclusion, the Board's approach would justify it in setting separate "need" rates for those routes which operate at a loss, without regard to the carrier's overall favorable financial position.²⁷ That was not the basis upon which Congress contemplated that subsidy mail pay would be given when it directed in Section 406(b) that such subsidy was to be awarded in an amount which, together with all other revenue, would meet "the need of each such air carrier."

offsetting excess earnings would have that effect. However, as pointed out *supra*, page 12, we do not challenge the Board's power to fix separately domestic and foreign rates. Nor do we contest the Board's practice of fixing class rates—a practice employed only for carriers on a service rate. Our sole attack is on the Board's refusal to offset excess domestic earnings in determining a carrier's subsidy need on its international division. The offsetting of such excess earnings would in no way preclude continued utilization of the comparison technique of rate making.

In any event, we submit that the policy considerations relied on by the Board could not possibly justify a finding—which the Board did not make—that C & S needed the additional \$654,000 within the meaning of Section 406(b).

²⁷ That such a possibility is not mere conjecture for purposes of argument is suggested by the situation that confronted the Board in fixing mail pay for Mid-Continent Airlines. Mid-Continent, a trunkline carrier, was temporarily certificated for a feeder route, which the Board required the carrier to treat as a separate entity for accounting purposes. *Parks Investigation Case*, Docket No. 3965, et al., Order No. E-4472, July 28, 1950, mimeographed pp. 25, 28. Subsequently the Board, in awarding temporary mail pay covering the feeder route, expressly provided that if the earnings from the rest of the carrier's operations exceeded a fair and reasonable return, "the excess may be offset against the mail pay need determined in the final mail rate proceeding" for the feeder route. *Mid-Continent Airlines, Mail Rates*, Docket No. 4680, Order No. E-4938, December 14, 1950. Although the Board there contemplated making the offset, economic policy considerations might, under the Board's theory in the instant case, dictate against the offset in some other similar situation.

CONCLUSION

For the foregoing reasons the order of the Board should be modified to reduce C&S's mail pay in the amount of \$654,000.

Respectfully submitted,

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JULY, 1952

APPENDIX A

Chicago and Southern—Domestic Services

REPORTED	1948	1949	1950	1948-1950 total
U. S. mail revenues received	\$1,891,989 ¹	\$1,800,384 ¹	\$1,747,319 ²	\$5,439,692
U. S. mail ton miles of traffic	481,731 ³	520,462 ³	608,040 ⁴	
U. S. mail revenues per ton-mile of U. S. mail	\$3.92 ¹	\$3.45 ¹	\$2.87 ²	
COMPUTATIONS				
If a mail service ton mile rate of	\$0.53 ⁵	\$0.53 ⁵	\$0.53 ⁵	
were applied, the resulting mail revenues would be:	\$255,317	\$275,845	\$322,261	\$853,423
Subsidy estimated by subtracting revenues computed on 53¢ ton mile rate basis from mail revenues actually received	\$1,636,672	\$1,524,539	\$1,425,058	\$4,586,269

Source:

¹ C.A.B. Recurrent Reports of Financial Data, C & S (Domestic Services), 4th Quarter of 1949.

² C.A.B. Recurrent Reports of Financial Data, Domestic Air Mail Carriers, Trunk Lines, 12 months ended 12-31-50, page 2 of 4.

³ C.A.B. Recurrent Report of Mileage & Traffic Data, C & S (Domestic Services), 4th Quarter 1949.

⁴ C.A.B. Recurrent Report of Mileage & Traffic Data, Domestic Air Mail Carriers, Trunk Lines, 12 months ended 12-31-50, page 2 of 4.

⁵ This 53¢ per ton mail rate was utilized by the Board in calculating C & S's subsidy in its Report on Administrative Separation of Subsidy from Total Mail Payments to Domestic Air Carriers, *supra*, note 15, and was applied by the Board in separating the carrier's service mail pay from subsidy. *Chicago and Southern Airlines, Domestic Operations*, Docket No. 5144, Order No. E-5869, November 15, 1951. There the Board, in fixing prospective annual mail pay of \$1,045,000, stated that \$382,000 represented service mail pay at 53¢ per ton mile, "and the balance of \$663,000 is subsidy." (*Id.* at mimeographed p. 7).

BRIEF FOR RESPONDENT

**United States Court of Appeals
for the District of Columbia Circuit**

No. 11,351

United States Court of Appeals
For the
District of Columbia Circuit

FILED SEP 26 1952

JESSE M. DONALDSON, POSTMASTER GENERAL OF THE UNITED
STATES, AND THE UNITED STATES OF AMERICA, ON BE-
HALF OF THE POSTMASTER GENERAL, *Petitioners*, **CLERK**

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

On Petition for Review of Orders of the Civil Aeronautics Board

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COUNTERSTATEMENT OF QUESTIONS PRESENTED

In respondent's view, the questions presented by this case are

1. Whether, after having established C. & S.'s domestic and international divisions as separate units for rate-making purposes and after having fixed a final rate for the domestic division in advance of the other, the Board had authority to subsequently refuse to offset the profits accruing under the final domestic rate against the carrier's need for mail pay for the international division, and, if so,

2. Whether the Board abused its discretion in refusing to offset the profits from the domestic division against C. & S.'s need for mail pay for its international division.

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United States Court of Appeals for the District of Columbia Circuit

No. 11,351

JESSE M. DONALDSON, POSTMASTER GENERAL OF THE UNITED
STATES, AND THE UNITED STATES OF AMERICA, ON BE-
HALF OF THE POSTMASTER GENERAL, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

On Petition for Review of Orders of the Civil Aeronautics Board

BRIEF FOR RESPONDENT

COUNTERSTATEMENT OF THE CASE

The Postmaster General seeks review in this case of an order entered by the Civil Aeronautics Board fixing mail pay for the international operations of Chicago and Southern Air Lines, Inc. (C. & S.) (J.A. 51). The single issue presented is whether the Board erred in refusing to reduce the allowance for mail pay for international operations by approximately \$654,000, the amount of "excess" profits which had accrued to C. & S. under a final mail rate for its domestic operations.

C. & S. conducts domestic operations over routes extending between Chicago and Detroit, on the one hand, and

Houston and New Orleans, on the other, and international operations over routes extending between Houston-New Orleans and Caracas, Venezuela via Havana and Kingston (See 9 C.A.B. 786, 789, 790, J.A. 7). The certificates of public convenience and necessity for both operations authorize the transportation of mail, and the carrier is entitled to compensation therefor at rates fixed by the Board pursuant to the provisions of Section 406 of the Civil Aeronautics Act (52 Stat. 998, 49 U.S.C. 486). These provisions authorize the fixing of "need" or subsidy mail rates for air carriers, and C. & S. was a "need" or subsidized carrier as to both its domestic and international operations at all times material to this case. Further, as is customary where a single carrier conducts both domestic and international operations of substantial size, different rates were prescribed by the Board for C. & S.'s domestic and international operations, and these rates were fixed in different proceedings before the Board.

C. & S.'s first international operations were inaugurated in 1946 (J.A. 8). At that time, the domestic operations were being conducted under provisional or temporary rates (See 9 C.A.B. 786, 789, 790). A temporary rate also was fixed early in 1947 for the international operations then being conducted (J.A. 8). On July 28, 1948, the Board established a final need rate for the domestic operations to be effective on and after January 1, 1948. *Chicago and Southern A. L., Mail Rates*, 9 C.A.B. 786 (1948). That order continued in effect at all times material to this case, and no petition for a new domestic rate had been filed either by the carrier or the Postmaster General. International operations continued under temporary rate orders until the entry of the order which is the subject of this review proceeding.

The order under review (J.A. 51) fixed final rates for the international operations for the past period November 1, 1946-December 15, 1950, and for the future period beginning December 16, 1950 (J.A. 59). For the past period, the one principally in issue, the Board determined the carrier's international "break-even need" (the amount neces-

sary to equalize income and outgo recognized for mail pay purposes) to be \$3,122,000 (J.A. 19). Return on investment at the rate of 7% was allowed in the amount of \$393,000 (J.A. 23). Actual income tax liability for the past period was determined to be \$147,000 and this amount allowed (J.A. 57). Thus, total mail pay for the past period was granted in the amount of \$3,662,000 (J.A. 58).

The Postmaster General contended before the Board, and contends here, that the mail pay allowance for the international operations should have been reduced by \$654,000. This sum represents the profits earned for the period 1948-1950 under the final rate for the domestic system in excess of a 7.4% return on investment. The domestic rate had been fixed at a level which would afford the carrier an opportunity to earn approximately 8% on investment under normal operating conditions, and the estimated rate of return on the basis of the carrier's predictions of future traffic had been 7.4%, *Chicago and Southern A. L., Mail Rates*, 9 C.A.B. 786, 812 (1948).¹ The domestic earnings or profits in excess of 7.4% were considered by the Postmaster General to constitute "other revenue" to the carrier to be taken into account in determining the amount of international mail pay which should be allowed, and, according to him, the Board mandatorily was required to offset these profits against the carrier's "need" for mail pay for the international operations.² The Board attorney assigned to the case was of the view that the offsetting of these earnings would constitute a forbidden recapture of earnings accrued under a final rate (J.A. 53). Without passing on the ques-

¹ Actually the domestic rate fixed in 1948 was a "sliding scale" rate designed to yield a higher return with increasing load factors, and the sliding scale was such that the carrier might either have lost money, or have realized a return on investment in excess of 13%, depending on load factors. Moreover, the Board advised C. & S. in fixing the rate that any economies in operations which might be achieved would "inure to the carrier in the form of higher earnings" (9 C.A.B. at p. 812). C. & S. in fact achieved operating economies. This factor, together with various accounting adjustments made in the depreciation account to reflect subsequent changes in the service life of DC-3 and DC-4 aircraft, resulted in a rate of return on investment for the period 1948-50 of 12.51% (J.A. 65).

² Section 406(b) (52 Stat. 998, 49 U.S.C. 486(b)) provides in part that, in fixing mail rates the Board shall consider, among other factors, the "need" of the carrier for subsidy mail pay in the light of "all other revenue of the air carrier."

tion of its power to make the offset (J.A. 21, 55), the Board held that in any event (J.A. 54)

. . . while we are required to take into consideration the need of a carrier for mail compensation together with "all other revenue", we believe that we are not required by Section 406(b) to reduce the carrier's mail pay with any part of such other revenue if there are sound reasons for not doing so as a matter of economic policy.

The Board concluded that as a matter of policy the offset contended for by the Postmaster General should not be made.

The Board explained the necessity and desirability for neither recapturing profits nor making up losses resulting from final divisional rates and of otherwise maintaining domestic and international operating divisions as separate rate-making units in appropriate cases, both for achieving the purposes of the Act and aiding the Board in the discharge of its duties. The Board stated that the statutory goal of a self-sufficient air transportation system can best be achieved by placing carriers on permanent rates under which the carriers will either retain the advantages of good earnings or bear any losses which may occur (J.A. 20). Final rates for both domestic and international operations cannot always be fixed simultaneously, as was true in this case. In such cases, the benefits which flow from placing carriers on final rates are such as to require the fixing of a permanent rate for one division in advance of the other, rather than retaining the carrier on temporary or open rates until such time as rates can be fixed simultaneously for both divisions (J.A. 20, 21). The Board also found that it is desirable to maintain the domestic comparative status between the domestic operators which have foreign routes and those which do not have foreign routes. Since carriers fall into fairly well-defined classes for domestic operations, the Board is enabled to fix uniform domestic mail rates for groups of carriers by excluding consideration of international operations. Such classification and comparative status provide a competitive incentive for

efficient operations, and also permit the Board to use comparative techniques in fixing rates (J.A. 54, 55).

Further, the Board stated that it is reluctant to burden the more "robust" domestic operations with the obligations of the "economically weaker" international operations of carriers engaged in both domestic and international operations, a burdening which will thwart the progress of the domestic operators toward self-sufficiency (J.A. 54). Keeping the domestic industry in a financially sound position will, the Board found, ultimately benefit the public in the form of lower fares, reduced mail compensation, more modern aircraft and improved operating methods (J.A. 54).

STATUTE INVOLVED

Pertinent provisions of the Civil Aeronautics Act of 1938, 52 Stat. 973, as amended, 49 U.S.C. 401 *et seq.*, relating to mail rates are set forth on pages 4 and 5 of the Postmaster General's brief. Other pertinent portions of the Act are cited or quoted at their appropriate place in the text of this brief.

SUMMARY OF ARGUMENT

I

Where domestic and international operating divisions of the same air carrier are established as separate rate-making units and a final rate established for one division in advance of the other, the Board is not thereafter mandatorily required to off-set profits accruing under the final rate against the carrier's minimum need for mail pay for the other division. Section 406(b) of the Act does not limit either subsidy payments or a carrier's "need" for subsidy to that minimum amount necessary to maintain an entire existing air carrier system as the Postmaster General erroneously contends. A carrier's "need" is merely one of several unweighted factors which the Board may consider in fixing mail rates. Further, the term "need" as employed in Section 406(b) expressly includes not only that amount of subsidy necessary to "maintain" a given operation but also that amount necessary to "continue the development

of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service and the national defense." The statutory concept of "need" thus embraces the extent of subsidy required to accomplish these developmental objectives.

II

Maximum operating efficiency and economy on the part of air carriers, and the development of air transportation, is promoted by placing and retaining the carriers on final mail rates under which the carriers either reap the benefits or stand the losses from future operations. Where carriers are comprised of both domestic and international divisions, final rates cannot always be fixed simultaneously for both divisions. In such cases, the benefits which flow from final rates are such as to require the fixing of a final rate for one division in advance of the other, and to justify a subsequent refusal to either offset profits or make up losses between the divisions, even though a carrier may on occasion obtain profits which otherwise would not inure to it. Moreover, the burdening of domestic operations with losses resulting from economically weaker international operations impedes the development of a sound air transportation system, and the maximum benefits which flow from the classifications of carriers established by the Board cannot be obtained unless international and domestic operations are retained as separate rate-making units in appropriate cases.

ARGUMENT

I. Where Domestic and International Divisions of the Same Carrier Are Established as Separate Units for Rate-Making Purposes, the Board Has Discretionary Power to Refuse to Offset Profits Accruing From One Division Against the Carrier's Need for Mail Pay for the Other Division.

In fixing mail rates for C. & S.'s operations and in refusing to offset profits from the domestic operations against the carrier's need for mail pay for the international operations, the Board adopted and gave effect to the familiar rate-making principle of establishing different op-

erating divisions of a carrier as separate units for rate-making purposes. The Postmaster General does not question the Board's power in appropriate cases to fix rates separately and at different times for different operating divisions of a single carrier (Br. p. 12), nor could he in view of the specific statutory authority conferred upon the Board in this respect and in the light of applicable case law.³ Neither does he raise any issue as to the reasonableness of the Board's action in establishing C. & S.'s international and domestic divisions as separate rate-making units and in fixing final rates for one division in advance of the other. Rather, the contention made on his behalf is that profits from one operating division mandatorily are required to be offset against need for mail pay for the other, and that the Board cannot lawfully award subsidy mail pay on a divisional basis for any given period of time in an amount which exceeds minimum operating need for the entire air carrier system during the period, irrespective of whether the operating divisions are established as

³ Section 416(a) of the Act (52 Stat. 1004, 49 U.S.C. 496(a)) empowers the Board to establish classifications of carriers according to the "nature of the services performed", and Section 406 authorizes the fixing "from time to time" of "different [mail] rates for different air carriers or classes of air carriers, and different classes of service." And apart from express statutory authority therefor, the determination of the proper unit for rate-making purposes is a matter committed primarily to administrative discretion. See e.g., *American Toll Bridge Co. v. Railroad Commission of California*, 307 U.S. 486, 494 (1939); *Illinois Commerce Commission v. United States*, 292 U.S. 474, 486 (1934); *Wabash Valley Electric Co. v. Young*, 287 U.S. 488 (1933); *Gilchrist v. Interborough Co.*, 279 U.S. 159, 209-210 (1929).

The Board has recently summarized its criteria for determining whether domestic and international operations shall be regarded as separate units or as a single unit for rate-making purposes as follows (*National Airlines Mail Rate*, Order Serial No. E-6344, dated April 21, 1952):

"There have been various criteria developed to guide the Board's determination of whether a single rate should be set for the foreign operations of a domestic carrier. One is the size of the foreign operation in relation to the total operations of the given carrier; another, the absolute size of the foreign operations; and a third, the extent to which the foreign operations are integrated with the domestic. To establish grounds for separate treatment it must be demonstrated that the foreign operations are large relative to the domestic operations of the carrier; that the foreign operations are so large that it would be neither practical nor feasible to attempt to set a system rate; and that the domestic and foreign operations are carried on more or less independently of each other."

C. & S.'s domestic and international operations are conducted by separate operating divisions and otherwise are such as to warrant their being treated as separate for rate-making purposes.

separate rate-making units or whether the profits involved accrued under a final or temporary rate order.⁴

The Board did not concern itself with the questions of whether the offsetting of C. & S.'s domestic profits would have constituted a forbidden recapture of profits accruing under a final unchallenged rate order, or whether after having elected to treat C. & S.'s divisions as separate rate-making units it lacked authority to offset profits and losses between them without first classifying the entire system as a single rate-making unit.⁵ Rather, the Board adhered to its practice of neither recapturing profits nor making up losses resulting from final divisional rates, upon findings that this practice and that of otherwise maintaining domestic and international operating divisions as separate for rate-making purposes is necessary to accomplish the purposes of the Act, and that the Board has discretionary authority to administer the mail pay provisions in such manner as to best develop a sound air transportation system even though that administration on occasion may require the allowance of subsidy mail pay in excess of mini-

⁴ The term "minimum operating need" as used in this brief refers to the Postmaster General's concept that subsidy mail rates for past periods must be limited to that amount necessary to meet operating expenses and to allow the customary rate of return on investment, and for future periods to a level which will afford the carrier a reasonable opportunity to earn no more than this amount.

⁵ In *Transcontinental & Western Air v. Civil Aeronautics Board*, 83 App. D.C. 358, 169 F. 2d 893 (1938), aff'd 336 U.S. 601 (1949), it was held that the Board lacked authority to fix rates retroactively to include a period in which a final rate was in effect and unchallenged, a course of procedure which the Board consistently had refused to follow on policy grounds. In that case, TWA's domestic operations were on final rates, whereas international operations were being conducted under temporary rates. TWA contended before the Board (J.A. in Case No. 9763, pp. 47, 48 and 89, 8 C.A.B. 685, 702, 703) and before this Court (TWA's brief in Case No. 9763, p. 22) that, irrespective of whether the Board otherwise had power to reopen the domestic rate for the past period, it nevertheless had power to reopen a part of the past period since *system* rates could be fixed from the beginning of international operations in that the Board is empowered to revise mail rates for an entire system retroactively to the time that any part of the system is on an open rate. This contention was rejected by the Board upon the basis that TWA's domestic and international operations were "separate units for rate-making purposes." 8 C.A.B. at p. 703. The Court affirmed the Board's action.

Had C. & S. sustained losses under the final domestic rate, an exact parallel to the TWA case would have been presented, and the Board would have lacked power to make up those losses in fixing the mail rate for the international operations. The question of whether a different rule prevails in the case of profits accruing under a final divisional rate, as the Postmaster General contends (Br. p. 14, n. 21), is irrelevant to the basis of the Board's decision in this case.

imum operating need.⁶ The Board clearly has such discretionary authority.

Section 406(b) does not limit subsidy payments to that minimum amount required to maintain an existing air carrier system, nor, as we demonstrate hereinafter, is the

⁶ Contrary to the Postmaster General's assertions (Br. p. 11) the Board's refusal to make the offset contended for did not represent a departure from prior Board precedents. It is true that the Board has stated in prior cases that "need" refers to the air carrier as a whole and not to geographical divisions. But these decisions did not purport to define "need" or to pass upon the question of whether mail pay could be awarded in excess of minimum operating need. Moreover, the cases relied upon by the Postmaster General dealt for the most part with the questions of whether, in rate cases where the entire system was the rate-making unit, mail pay could be allowed for all operations rather than being restricted to those schedules and routes over which mail was transported, or whether different rates should be fixed for the different routes which collectively made up the system rate-making unit. In these cases, the Board held that mail pay could be allowed in an amount sufficient to sustain the entire operation, and that different rates should not be fixed for different routes. *Chicago and Southern Air Lines, Mail Rates*, 3 C.A.B. 161 (1941); *Delta Air Corporation, Mail Rates*, 3 C.A.B. 261 (1942); *Eastern Air Lines, Mail Rates*, 3 C.A.B. 733 (1942); *Pennsylvania Central Airlines, Mail Rates*, 4 C.A.B. 22 (1942).

Although fixing mail rates on a system basis wherever possible, the Board nevertheless has heretofore treated foreign and international divisions as separate entities for rate-making purposes in appropriate cases. Further, it has made specific pronouncements with respect to the problem herein involved in two earlier cases. In the case of the domestic and international divisions of TWA, it held that "TWA's domestic and international operations are separate units for rate-making purposes" and that it lacked power to make up TWA's large losses under a final domestic rate in fixing rates for its international operations. *Pennsylvania Cent. Air Et Al, Motions*, 8 C.A.B. 685, 703 (1947), *aff'd Transcontinental & Western Air v. Civil Aeronautics Board*, 83 App. D.C. 358, 169 F. 2d 893 (1948); 336 U.S. 601 (1949). In *Pan American Airways, Latin-American Rate Case*, 3 C.A.B. 657 (1942), the Board determined that Pan American's mail rates for its Latin American Division had resulted in excess profits during the period between the institution of the rate proceeding and its decision therein. Rather than requiring a refund from the carrier, which it clearly could have done, the Board refused to recapture these profits upon "economic considerations and considerations of policy" (3 C.A.B. at p. 668). However, repeating its statement in the *Chicago and Southern Case, supra*, that "need" embraced the needs of the air carrier system rather than geographical divisions, it stated that it would take these excess profits into account in determining the carrier's "need" for mail pay for its other divisions. The proceeding was reopened on reconsideration (6 C.A.B. 85), and final rates fixed simultaneously for all of Pan American's divisions (6 C.A.B. 59, 61, 83, 85). No additional subsidy payments were made since the excess payments for the Latin-American Division which were subject to recapture were more than enough to meet the carrier's "need" for all of its divisions. 6 C.A.B. at p. 78.

The TWA case and the instant case demonstrate that where a final rate is established for one division in advance of the other, the Board will neither make up losses nor offset profits resulting from the final division rate. The *Pan American* case demonstrates that, where excess payments made under temporary rates are discovered in advance of or simultaneously with the fixing of a final rate for another division, the Board may require the carrier to offset these excess payments against its "need" for the other divisions rather than itself recapturing the excess payments and then directly making up the "need" for the other divisions.

statutory concept of "need" so limited.⁷ But even if the Postmaster General is correct in his interpretation of need, Section 406(b) plainly provides that need is merely one unweighted factor to be taken "into consideration, among other factors," in fixing mail rates. The other factors which may be taken into account obviously include the overall developmental responsibilities placed upon the Board.⁸ In this view of the case, the situation here presented is similar to and should be controlled by *Secretary of Agriculture v. Central Roig Refining Co.*, 338 U. S. 604 (1950). There the Secretary was directed and empowered to make a determination of sugar quotas upon consideration of three named but Congressionally unweighted factors. The Secretary "considered" all three factors, just as

⁷ Section 406(b) (52 Stat. 988, 49 U.S.C. 486) provides in pertinent part:

"In determining the rate in each case, the Board shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense."

⁸ The Congressional mandate of policy contained in the Act (Section 2, 52 Stat. 980, 49 U.S.C. 402) provides:

"In the exercise and performance of its powers and duties under this Act, the Board shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity—

(a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by, air carriers.

(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

(d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(e) The regulation of air commerce in such manner as to best promote its development and safety; and

(f) The encouragement and development of civil aeronautics."

the Board considered in this case whether it should offset the domestic profits against C. & S.'s international need, but concluded that one factor should not be applied and therefore should not be given weight. In sustaining the Secretary's action, the Court stated (338 U. S. at pp. 611, 612):

. . . he is under a duty merely to take "into consideration" the particularized factors. The Secretary cannot be heedless of these factors in the sense, for instance, of refusing to hear relevant evidence bearing on them. But Congress did not think it was feasible to bind the Secretary as to the part his "consideration" of these three factors should play in his final judgment—what weight each should be given or whether in a particular situation all three factors must play a quantitative share in his computation.

Moreover, the statutory concept of need is not limited to that amount of subsidy necessary to maintain operations over a given air carrier system. On the contrary, the term need as employed in Section 406(b) expressly includes not only that amount of subsidy necessary to "maintain" a given operation, but also that amount necessary to "continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense." The extent of a carrier's need thus is the extent of subsidy required to accomplish these developmental objectives on either a divisional or system basis, and the powers conferred in administering the mail pay provisions of the Act obviously were designed and intended to be co-extensive with the overall developmental responsibilities placed upon the Board. Due regard for the developmental directives contained in the Act has been recognized by the Court to be "peremptory" upon the Board in certificate cases,⁹ and should be recognized as being equally peremptory in mail rate cases.

The Board has always considered that it has statutory authority, as it does, to allow subsidy mail pay in excess of minimum operating need where reasons of economic

⁹ *American Airlines v. Civil Aeronautics Board*, — — App. —, 192 F. 2d 417, 420 (1951).

policy require that action for the furtherance of the statutory goal of a sound and economically self-sufficient air transportation system. Thus, the Board has long employed "sliding-scale" need mail rates which have the effect of yielding a higher return on investment with increasing load factors or decreasing costs, thereby encouraging and rewarding carriers for efficient promotional activity and efficient operations. The Board has refused in several past instances to require carriers to refund mail payments which clearly were subject to recapture because the refunding of those payments would impede the progress of the carrier toward the goal of economic self-sufficiency. *Pan American-Grace Airways, Mail Rates*, 3 C.A.B. 550, 564 (1942); *Pan American Airways, Latin American Rate Case*, 3 C.A.B. 657, 668 (1942); *American Airlines, Mail Rate Proceeding*, 3 C.A.B. 770, 776 (1942). The Board also has refused to offset against a carriers' "need" a portion of the profits derived from a route transfer for the purpose of encouraging other voluntary route transfers required for the development of a sound air transportation pattern. *Western Air Lines, Mail Rates*, Order Serial No. E-5467, dated June 26, 1951.¹⁰

Further, the Board is empowered by Section 406 to fix uniform rates for "classes of air carriers, and different classes of service." This power, recognized by the Supreme Court as an important regulatory device for securing the benefits of competition (*Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601, 606-7 (1949)), cannot be effectively exercised unless the Board is permitted to continue its practice of treating domestic and international operations as separate rate-making units. Further, under any given class rate, some carriers obviously will receive less than their operating needs, whereas others will receive more. In such cases, it might be cheaper to the government to pay each carrier strictly according to its own operating need but it can hardly be argued that the Board is required to subjugate the develop-

¹⁰ This order is presently under review in *Donaldson, et al. v. Civil Aeronautics Board*, U.S. App. D.C., Case No. 11,259.

ment of a sound air transportation system through traditional competitive concepts to this factor.

Thus, the entire purpose and focus of "need" payments are not simply to make a carrier financially whole in the usual sense, but to develop an air transportation system to serve paramount national interests. The Board's refusal to make the offset contended for by the Postmaster General must be evaluated in the light of the meaningful purpose of the mail pay provisions of the Act. If the Board is to accomplish its objectives, it cannot administer those provisions in the manner of a public relief law.

II. The Board Did Not Abuse Its Discretion in Refusing to Offset the Profits From C. & S.'s Domestic Division Against the Carrier's Need for Mail Pay for Its International Division.

Maximum operating efficiency and economy on the part of air carriers obviously is promoted by placing and retaining them on final mail rates under which the carriers either reap the benefits or stand the losses from future operations, irrespective of whether those final rates are "need" or "service" rates. Moreover, the Act contemplates that wherever possible carriers shall be required to operate under such final rates rather than on a cost-plus basis. *Transcontinental & Western Air v. Civil Aeronautics Board*, 336 U. S. 601 (1949). Because of differing conditions existing in the domestic and international field, it is not always feasible for the Board to fix a single mail rate for carriers comprised of domestic and international operating divisions, and separate final rates often may be established for one division in advance of the other (J.A. 20). In cases which involve need rates for both divisions, the Board either may retain the carrier on a temporary rate or "cost-plus" basis as to its entire operations until such time as final rates may be fixed simultaneously for both divisions, thereby avoiding the problem of offsetting profits here involved, or it may fix a final rate for one division in advance of the other for the purposes of obtaining the benefits which result from final rates to the greatest extent practicable, even though the carrier as a result of that action

may obtain mail pay which otherwise would not inure to it.¹¹

The Board reasonably has elected in such cases, as in this case, to follow the second alternative, not only because of the benefits which flow from placing carriers on final rates but also because of the overall desirability for maintaining domestic and international operating divisions as separate rate-making units in appropriate cases. The reasonableness of the Board's policy in this latter respect is best demonstrated against the background of the situation existing with respect to carriers engaged in both domestic and international operations.

Four of the fourteen domestic trunk lines (TWA, Braniff, C. & S. and Northwest) presently are engaged in both domestic and international operations which are classified as separate units for rate-making purposes.¹² Of these four, all but C. & S. are paid at compensatory rates for domestic operations. Domestically, TWA is classified with American, Eastern, and United as the "Big Four" carriers paid at the lowest service mail rate for domestic operations, presently 45 cents per ton-mile. Braniff and Northwest are classified for domestic operations with four other domestic carriers (Capital, Delta, National and Western) as falling within the group of carriers paid at a service rate of 53 cents per ton-mile. C. & S. also has been classified by the

¹¹ We recognize that under the Postmaster General's views a third alternative is presented, that of fixing a final rate for one division in advance of the other and placing the risks of future losses on the carrier but at the same time retaining for the benefit of the government the advantages of any possible future profits. Whatever may be the legal power of the Board in this respect, it has not yet chosen to follow this possible third alternative. Moreover, it is apparent that this course of action would not provide the same spur to efficient operations as is provided by allowing the carrier to retain the benefits of profitable operations. Indeed, a carrier would have little incentive to achieve economies during the period which intervenes between the fixing of a final rate for one division and a final rate for the other. On the contrary, it would be to the carrier's advantage to conduct its affairs in such manner as to minimize the profits which otherwise would be recaptured.

¹² Five other carriers (American, Eastern, United, National, and Colonial) conduct foreign or overseas operations which in the past have been regarded as separate units for rate-making purposes but which presently are regarded as "stub-end" operations sufficiently integrated with domestic operations so as to make feasible the fixing of rates on a system basis. See C.A.B. publication "Administrative Separation of Subsidy from Total Mail Payments to United States International, Overseas and Territorial Air Carrier," 1952, pp. 7 & 8.

Board as comparable with these six carriers for service mail rate purposes and it is hoped that C. & S. will in the future be placed on a service rate of 53 cents per ton-mile.¹³ Uniform class mail rates as yet have not been established in the international field. Nevertheless, the Board has classified international operations for comparative rate-making purposes. TWA's international operations are classified as comparable to those of Pan American's Atlantic Division and Northwest's with Pan American's Pacific Division. The international operations of C. & S. and Braniff are grouped with those of Panagra.¹⁴

The percentage of subsidy to total mail payments is substantially greater in the international field than in the domestic field, and the Board has estimated that the level of subsidy support for international operations will tend to increase over the next several years.¹⁵ On the other hand, those domestic trunk line operations which still require subsidy support appear to be well on the road to economic self-sufficiency.¹⁶

The Board has heretofore determined that the public interest requires the participation of more than one American flag carrier in the international field. *American Export Air., Transatlantic Service*, 2 C.A.B. 16 (1940); *Northeast Air. Et Al., North Atlantic Routes*, 6 C.A.B. 319 (1945). The selection of domestic carriers to perform international services benefits international operations in that existing experienced headquarters staffs, trained operation crews and workers, and shops for the maintenance and repair of aircraft can be utilized in both operations. *Northeast Air. Et Al., North Atlantic Routes, supra*, 6 C.A.B. at pp. 326-327. The use of these existing facilities, and the spread of

¹³ See C.A.B. Publication "Administrative Separation of Subsidy from Total Mail Payments to Domestic Carriers," 1951, p. 14.

Braniff, C. & S., Northwest, Capital, Delta and Western for many years were classified as the "Little Six" domestic carriers for service mail rate purposes.

¹⁴ See C.A.B. Publication "Administrative Separation of Subsidy from Total Mail Payments to United States International, Overseas and Territorial Air Carriers," 1952, p. 7.

¹⁵ *Ibid*, p. 4.

¹⁶ See C.A.B. Publication "Administrative Separation of Subsidy from Total Mail Payments to Domestic Air Carriers," 1951, p. 7.

overhead costs made possible thereby, often enables both domestic and international operations to be performed more economically by carriers engaged in both types of operations than would be possible if the operations were conducted by entirely separate carriers. Moreover, where consistent with the various other criteria which the Board must consider, the Board will select to operate a given route that carrier which can provide a single-carrier and therefore a more convenient service to the largest portion of the traveling public. *Additional Service to Latin America*, 6 C.A.B. 857, 900 (1946). The certification of domestic carriers for international operations will provide maximum single-carrier service to foreign points in most cases, and C. & S. was certificated for its Latin American routes largely because it could provide a "single-carrier operation connecting the important cities of the Mississippi Valley and the Great Lakes region with points in the Caribbean and on the north coast of South America." *Additional Service to Latin America*, *supra*, 6 C.A.B. at p. 910.

TWA, Braniff, C. & S. and Northwest compete domestically with other trunk line carriers engaged only in domestic operations, many of which either do not require subsidy support or are rapidly approaching that stage. Commercial rates must be maintained for competitive reasons at approximately the same level for the domestic trunk line carriers. Assuming that the domestic fare structure is or could be established at a level which would enable domestic operations to support all or a part of international operations and that the Board should require such support, then carriers engaged in both types of operations obviously would not obtain the same rate of return on investment that wholly domestic carriers would earn. Under these circumstances, domestic carriers would be reluctant to conduct or expand international operations, with a consequent loss of the operating experience and economies and convenient freight, passenger and mail service which they can bring to the international field. Moreover, the Board is of the view that any excess earnings in the domestic field should be used either for improved domestic services, or

as the basis for reducing domestic commercial rates with new impetus to the further development of the industry (J.A. 54), a determination within a field committed to the competence of the Board and entirely reasonable.

Actually, it is unlikely that domestic operations will be able to support international operations in the immediate future. On the contrary, as the Board found, the carrying of international operations on the back of domestic operations would be "subjecting the latter to an unjustifiable strain" and would merely serve to impede the progress of domestic operations toward economic self-sufficiency (J.A. 54). Under these circumstances, and in any event under the Board's view that domestic commercial rates should be fixed at a level necessary to sustain only domestic operations, those carriers engaged in both domestic and international operations presently must be subsidized as to their international operations. The treatment of the entire air carrier system rather than the operating division as the rate-making unit would mean only that these carriers would then be subsidy or need carriers on a system rather than on a divisional basis.

This result would not carry any attendant benefits since the Board's policy of establishing domestic and international operating divisions as separate rate-making units and of fixing final rates for one division in advance of the other need not result in excessive profits to carriers to any greater extent than where carriers are placed on final system rates. Indeed, the Board's policy will result in savings to the government where losses are experienced by a carrier under a final divisional rate. Either excess profits or substantial losses are possible under any final rate, and it is for this reason that rates are not immutable. If a final divisional rate embodies subsidy payments and the profits thereunder prove excessive, then both the Board and the Postmaster General are free to institute proceedings for a lower divisional rate just as in the case of a system rate. Section 406(b).¹⁷

¹⁷ A domestic divisional rate lower than the one here involved subsequently has been established for C. & S. See J.A. 53. The Board maintains constant

The foregoing considerations clearly outweigh the short term benefit which would have resulted from recapturing the sum of money here involved. Further, adoption of the offset principle would have impaired the Board's existing classification system since carriers engaged in both domestic and international operations would then be required to be regarded for many purposes as one air carrier system. This impairment would have precluded the Board from obtaining the maximum benefits which flow from the classifications which it has established, including those of comparative rate-making techniques. The Board did not abuse its discretion in refusing to accede to the principle for which the Postmaster General contends.

CONCLUSION

Upon the basis of the foregoing reasons and authorities, the Board's order should be affirmed.

Respectfully submitted,

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scrutiny over the earnings of carriers under final mail rates, and institutes proceedings for the fixing of lower rates if and when it becomes apparent that the existing rate is too high. Pursuant to this policy, new rate proceedings were instituted by the Board during fiscal year 1952 for the reduction of the mail rates of nine air carriers. Five such proceedings had been instituted during fiscal year 1953 up to the time of the preparation of this brief, including a proceeding for the reduction in the international rate for the future period established for C. & S. in this case.

It is obvious, of course, that a reasonable and representative period of time must elapse before it can be determined whether a particular rate is providing excess earnings since air carrier revenues are subject to the same fluctuations that exist in other fields.

**BRIEF FOR CHICAGO AND SOUTHERN AIR LINES,
INC., INTERVENOR.**

United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

No. 11,351

JESSE M. DONALDSON, Postmaster General of the United States, and THE UNITED STATES OF AMERICA on behalf of the Postmaster General, *Petitioners*,

v.

CIVIL AERONAUTICS BOARD, *Respondent*.

**On Petition for Review of Order of the
Civil Aeronautics Board.**

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COUNTERSTATEMENT OF QUESTIONS PRESENTED.

In intervenor's opinion, the questions presented by this case are:

- (1) Does the Civil Aeronautics Board have discretionary authority to establish separate operating units or divisions within a single company for rate-making purposes?
- (2) If the answer to (1) is in the affirmative, and in the exercise of such discretion the Board has in fact separated a carrier's international and domestic divisions for rate-making purposes and has established a final rate for the domestic division in 1948, in establishing the proper rate for the international division in 1951 is the Board legally empowered to offset a portion of the earnings of the domestic division under a final and unchallenged rate against the requirements of the international division?
- (3) If the answer to (2) is in the affirmative, is the Board's power to offset discretionary or mandatory?
- (4) If the answer to (3) is that the power is discretionary, has the Board abused its discretion in refusing to offset in this particular case?

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United States Court of Appeals

FOR THE DISTRICT OF COLUMBIA CIRCUIT

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CIVIL AERONAUTICS BOARD, *Respondent*.

On Petition for Review of Order of the
Civil Aeronautics Board.

BRIEF FOR INTERVENOR.

COUNTER-STATEMENT OF THE CASE.

Chicago and Southern Air Lines, Inc., was granted leave to intervene in this proceeding by order of this Court entered April 21, 1952.

The Civil Aeronautics Board, in July of 1948, fixed final mail rates effective January 1, 1948 for the operations of Chicago and Southern Air Lines, Inc. over its domestic routes. When fixing the final domestic mail rates, the

Board established a rate which it estimated would return the carrier a minimum of 7.4 percent on that portion of the carrier's investment properly allocated to its domestic operations. The final rates so established for the domestic division remained in effect and unchallenged during each of the years 1948, 1949 and 1950. The domestic rate after 1950 is not in issue in this case. For the period 1948-1950, the domestic routes of the carrier under the final mail rates prescribed by the Board yielded an average return on investment estimated at 12.5 percent. The Postmaster General contends that the post 1948 earnings over and above the *minimum* return of 7.4 percent estimated by the Board in establishing the domestic mail rate are "excess earnings". This erroneous characterization is inconsistent with the Board's decision in the 1948 *C & S Domestic Mail Rate Case*.¹ In that case the Board specifically held that a 7.4 percent return was not to be considered a ceiling and declared that any economies which the carrier's management succeeded in accomplishing would inure to the carrier in the form of higher earnings.

In an Opinion and Order issued on October 18, 1951 the Board fixed final mail rates for the Latin American operations of Chicago and Southern Air Lines, Inc. The carrier contended in the case before the Board (a) that the Board did not have the power to offset in the international rate case the earnings established three years earlier under the final domestic mail rate, and (b) that even if such power to offset did exist, the Board's power was discretionary rather than mandatory and that sound arguments of economic and regulatory policy argued against the imposition of such an offset. The Board did not rule directly on its legal power to offset but, assuming such a power, held that in the exercise of its discretion it found that sound reasons against offset did in fact exist. The Postmaster General challenges both the carrier and the Board, arguing that under the statute the requirement that the Board offset is

¹ 9 CAB 786 (1948).

mandatory. He contends that under Section 406(b) the Board must, as a matter of law, offset the profits from earlier years derived from the carrier's domestic operations in fixing and determining the rates of compensation for the carrier's transportation of mail over its Latin American routes and had no statutory authority to exercise a discretionary judgment in the matter.

STATUTES INVOLVED.

The pertinent provisions of the Civil Aeronautics Act of 1938, 52 Stat. 977, as amended, 49 U. S. C. 401 *et seq.* are set forth in full in the appendix hereto.

SUMMARY OF ARGUMENT.

I.

The Board is legally empowered to establish separate rate-making units within a single company for rate-making purposes. The Board did not err in determining that C & S' domestic and international divisions constituted two separate rate-making units. As a regulatory agency it is vested with discretion to select an appropriate rate-making unit on a case to case basis. This is so especially where, as here, the carrier rendered two distinct types of service. The treatment of C & S' international division as a rate making entity separate and apart from the domestic division was authorized by the Act. Section 406(b) of the Act expressly authorizes the Board to fix different rates for different classes of carriers after considering the conditions peculiar to that class of air carrier. Section 801 of the Act also recognizes the basic difference between domestic and international air operations. The Board's judgment that each division should stand on its own feet and bear its own burdens was not only authorized but contemplated by the Act.

II.

Aside from the Board's statutory authority to treat C & S' Latin American operation as a separate carrier for rate-making purposes, there exists ample support from a practical policy standpoint. The United States carriers must be given every advantage and opportunity to compete on the same level and under the same conditions with foreign flag air carriers or else the efforts of the United States lines to engage successfully in foreign air transportation would be effectively thwarted. If the domestic service of a United States carrier is to be burdened with the losses of its foreign service, the natural tendency would be for present United States air carriers to discontinue entirely or seriously curtail existing foreign service. It would also discourage other domestic carriers from even entering the foreign field. The Board's judgment in treating the carriers international division as a separate rate-making unit was a fair and reasonable exercise of discretion.

III.

Having established separate international and domestic divisions of C & S for rate-making purposes, and having established final and permanent rates for the domestic division in 1948, the Board is not legally empowered to offset allegedly excessive earnings of the domestic division under the final and unchallenged 1948 domestic rate in establishing proper rates for the international division in 1951.

The offset of such earnings would have the effect of retroactively revising the closed and permanent domestic rate. The Board has no express or implied jurisdiction to revise rates retroactively or to disturb past earnings. An attempt to revise rates retroactively through a policy of offset would prevent air carriers from being placed on permanent rates and would lead to a cost-plus basis of rate-making. The cost-plus basis would not harmonize

with the clear purposes of the Act. It would violate the traditional concepts of rate-making. The language of the Act nowhere suggests that Congress intended to break with the traditions of rate-making.

IV.

If the Board is legally empowered to effect such an offset of domestic profits in establishing proper rates for the international division, the Board's power is discretionary rather than mandatory.

Under Section 406(b) of the Act, the Board is not *required* to offset past earnings but is only *required to consider* such earnings among "other factors" in fixing fair and reasonable rates. The Act vests in the Board the discretionary power to include or not to include "other revenues" where such action in its expert judgment will best effectuate statutory policy. Congress did not limit the Board in fixing fair and reasonable rates to the minimum amount necessary to maintain an existing operation, but empowered the Board to fix a mail rate that would provide for incentive and development of air transportation.

V.

The Board has not abused its discretionary authority in refusing to offset domestic profits of the carrier. On the contrary the conclusion of the Board not to adopt the offset policy was reasonable and proper and fully warranted in view of important economic and policy considerations. The Postmaster General can not quarrel with the Board's objective to place air carriers on self-sufficient basis as rapidly as possible. This objective, in the judgment of the Board, can best be obtained by placing carriers on a permanent mail rate. A policy of offset would unquestionably destroy the permanency of a rate because the carrier would not know from one accounting period to another how much of its earnings it would be allowed to retain. Without a per-

manent rate there would be no incentive to maximum economy and efficiency in airline operations. Permanent rates should be inviolable until adjusted as to future periods through due process after notice and hearing.

If the offset policy were adopted, thus permitting the Board in effect to recapture past earnings on domestic operations under permanent mail rate order, great financial confusion would result. Investors would be misled, ability to attract capital would be impaired, no dividend declaration would be secure and no offering of securities would have a firm foundation.

It would also be contrary to the public interest to burden the robust domestic operation with the economically weaker international operation. The imposition of such burden would postpone indefinitely the desirable objectives of lower fares to the public, the acquisition of new and modern aircraft, the installation of new and modern safety devices, and generally, the attainment of self-sufficiency. Rather than be burdened with unprofitable international operations, the United States domestic carriers would withdraw from the international field to the advantage of the foreign flag carriers and to the detriment of the national defense and the Postal Service.

The adoption of the offset policy is undesirable from an administrative standpoint because it would prevent the Board from preserving a comparative status between domestic operators which have foreign routes as against those which do not have foreign routes. The advantages of the comparative technique of analysis in rate-making are manifold and indispensable. Without it the Board would have no safe guide to chart its course in performing its rate-making functions.

The adoption of the offset policy resulting in a recapture of past earnings over a substantial period of time is contrary to established Board policy and justice and equity forbid confiscation of profits earned under a permanent rate when losses under a permanent rate are not recoverable by the carrier.

VI.

The Court should give great weight to the construction placed upon a statute by an administrative agency charged with the responsibility for the administration and enforcement of the statute. The Board's long record of practical experience with air transportation entitles its judgment to persuasive consideration by the Court. The Board is in a better position than a reviewing Court to determine appropriate applications of a statute which it is directed to administer. The construction of Section 406(b), urged by the Board and the carrier is consistent with the intent of Congress and the language of the Act. It has a reasonable basis in law and should be binding upon this Court in its review of the Board's Order of October 18, 1951.

ARGUMENT.**I.****THE ACT CONFERS DISCRETIONARY POWER ON THE BOARD TO DETERMINE APPROPRIATE UNIT FOR RATE-MAKING PURPOSES.**

The Postmaster General contends that the Board has no authority under the Act to "compartmentalize" the carrier for mail rate purposes. It is well settled that the Board, in common with other regulatory agencies, enjoys primary administrative discretion to determine the appropriate unit for rate-making purposes.

The clear mandate of Section 406(b) of the Act which requires that mail pay shall be awarded in an amount corresponding to the statutory "need" for such compensation as a means of maintaining and continuing the development of air transportation in the public interest will only be met by a determination that C&S domestic and international divisions constitute two separate rate-making units.

The treatment of an international division as a rate-making entity, separate and apart from the treatment of

a domestic division, is both desirable and necessary and is authorized by the Act. The first sentence of Section 406(b) authorizes the Board to fix different rates for different classes of service after considering the conditions peculiar to that class of air carrier. It necessarily follows that if the Board has the power to fix the international division as a separate rate-making unit it could, by virtue of the nature of such power, exclude domestic earnings in establishing international rates in the instant case. The domestic and international divisions of C&S have always been regarded as separate and independent rate-making units because the standards applicable to one are not necessarily applicable to the other.

The Board's administrative interpretation of the Act is in line with the fundamental tenet of public utility law that regulatory agencies are vested with discretion to select an appropriate rate-making unit on a case-to-case basis. C&S is rendering two distinct services—domestic transportation by air and international air transportation. The Latin American air routes are not used or useful to render any service covered by the domestic operations. The carrier's duty to operate either service is independent of its obligation to operate the other.²

Segregation of operations by the same company in fixing rates for separate departments or services of the company has been followed in many rate-making proceedings and upheld by the courts.³

The Michigan Public Service Commission, in an investigation of the rates and charges of the Detroit Edison Company upon a petition of the City of Detroit,⁴ rejected the contention of the company that its steam-heating business was an essential adjunct to its electric business, and that the two services were so interconnected and interdependent that it was impossible to consider the facilities of the

² *American Toll Bridge Company v. Railroad Commission of the State of California*, 307 U. S. 486, 83 L. ed. 1414.

³ *Re Ohio Bell Telephone Co.*, 2 PUR (N. S.) 113, 623.

⁴ *Detroit vs. Detroit Edison Co.*, 59 P. U. R. (N. S.) 1.

two departments separately, and that they should be considered as one integral utility for rate-making. The Commission found that the steam-heating business was separable and that it should be so treated. The Commission said:

"It is a fundamental principle of utility regulation that each type of utility service should be self-sustaining. *It is inequitable to allow the losses of one type of service to become a direct burden upon another type of service.* It does not appear appropriate that the steam heating division of the company should be consolidated with the electric division." (Emphasis supplied).

In *Southwestern Bell Teleph. Co. v. City of San Antonio*, 2 F. Supp. 611, a proceeding involving an alleged confiscatory rate ordinance affecting the City of San Antonio, it was held that the telephone company doing a state and interstate business must segregate its properties, revenues and expenses relating to the city service from those relating to the balance of its services. The Court said that the issue for determination *was not whether the company was earning an adequate net revenue on its entire properties, but whether the rates fixed for local exchange service in San Antonio were sufficient to permit the plaintiff to earn a fair return on its property devoted to the public use within the jurisdiction of the city.*

Where a company renders distinct types of service, the earnings of each department must be considered separately upon its own merits and rates must be determined for each department and be reasonable *per se*. The company cannot offset a deficiency in return from one business as against an excess in return from its other business, but each department must stand on its own foundation and bear its own burdens.⁵

In the light of all the facts and circumstances, the fixing of rates by the Board for the international air mail

⁵ *Re Syracuse Lighting Co.*, 30 P. U. R. (N. S.) 385.

operations of the carrier without offsetting the earnings from the carrier's domestic business was consonant with the principle that where a company is rendering two distinct types of service, each service should be treated separately for rate-making purposes. This basic principle of rate-making has never been foreign to the Board's thinking on the problem. The Board has frequently declared that, having once fixed final rates for one division of an air line, on the assumption that such division is a separate unit for rate-making purposes, this prior classification may not be retroactively invalidated by later inconsistently characterizing a second division of the same airline as a member of a joint or system rate-making unit.⁶ That the Board has no authority to retroactively revise a final rate is discussed in Part III, *infra*.

The Postmaster General contends that the Board's decision in the instant case departs from its prior consistent construction of the Act to the effect that the need referred to in Section 406(b) is that of the air carrier as a whole and not that of any particular geographical division of its operations. In support of this contention Petitioner has cited, at page 11 of his brief, six decisions of the Board rendered in 1942 and 1943. An examination of these cases discloses that the decisions related to carriers which were either wholly domestic or wholly international operations. None of the cases cited by Petitioner, including the *Pan American Mail Pay Case* in 1944,⁷ dealt with a carrier that had both domestic *and* international operations. None of these cases, therefore, are authority for the proposition that the Board is scrapping "a long standing and heretofore consistent construction of the Act."

Aside from the fact that none of the case cited by Petitioner support his contention that the need referred to in Section 406(b) is that of the air carrier as a whole and not that of any particular geographical division of its op-

⁶ *Pennsylvania Central Airlines Corporation, et al., Motions*, 8 CAB 685, 703 (1947).

⁷ *Pan American Airways, Alaska Mail Rates*, 6 CAB 61, 67.

eration, it must also be pointed out that in the cited cases the rates for the different routes or divisions were *open*. For example, in the *Pan American Mail Pay Case, supra*, the Board said that because of excessive earnings in the Latin American division, the Alaskan Division would be given compensatory mail pay only and would not be given sufficient mail pay to result in earnings on the investment properly allocated to the Alaskan division alone. However, in that case the rates for both the Latin American division and the Alaskan division were *open*, both divisions being on *temporary* rates and neither division was on a *permanent* rate. In the instant case, while the Latin American division rate was open, the domestic division rate was *closed* and had been closed since 1948. What the Board can or should do where the mail rate was temporary and open is entirely different from what the Board can or should do when the mail rate is closed and permanent.

The Board's decision in the instant case does not fly in the face of any specific directive in Section 406(b) but, on the contrary, was not only contemplated but authorized. The expert judgment of the Board, after considering all factors, things and conditions, should not be lightly set aside. Congress has delegated certain duties and responsibilities to the Board and requires it to exercise a rational judgment upon certain facts in order to ascertain public interest, convenience and necessity. As this Court aptly said in *American Airlines v. Civil Aeronautics Board*, 192 F. 2d 417, 420:

"It is in the exercise of that sort of judgment that the much discussed expertise of administrative agencies, finds its greatest value. Here is the field of uncertainties, imponderables and estimates. This is where the rule that a conclusion within the realm of rational deduction or inference stands despite difference of opinion, has its greatest applicability."

II.

TREATING THE CARRIER'S INTERNATIONAL DIVISION AS A SEPARATE RATE-MAKING UNIT WAS PROPER AND JUSTIFIED.

The Board committed no error in viewing C&S' Latin American operation as a separate carrier for rate-making purposes. As pointed out above, it not only possessed statutory authority, but also enjoyed administrative discretion to do so. We agree with the Board that as a practical matter it was desirable to treat the international division separately.

In the Board's "Statement of Tentative Findings and Conclusions" (J. A. 20) it acknowledged its responsibility to place carriers on final future rates as rapidly as possible. The task of placing a carrier with both domestic and international divisions on final future rates is an exacting one, and much more difficult than in the case where the carrier operates solely in the domestic or solely in the international field because many of the considerations which enter into the fixing of an international rate are different from those entering into the establishment of a domestic rate. Congress recognized the basic differences between domestic and international operations by providing in Section 801 of the Act that any certificate authorizing an air carrier to engage in "overseas or foreign transportation" shall be subject to the approval of the President. The President's approval is not required with respect to purely domestic operations. In other words, Congress, by requiring approval of the President before a certificate authorizing overseas transportation could be issued, gave formal recognition to the fact that a distinction existed between domestic and international air transportation. The basic reasons underlying the enactment of Section 801 of the Act are present and equally applicable *in fixing rates* for the transportation of mail on an international division, and fully justify the Board in

treating the international division as a separate rate-making unit and determining its need without offsetting past earnings of the carrier's domestic division.

The Court may well take judicial notice of the competition encountered by United States air lines in foreign transportation and particularly competition from air lines of foreign governments. These foreign air lines are not subject to the same degree of control and regulation in conducting air transportation to and from points in the United States as are the lines of the United States. Necessarily, therefore, the air lines of the United States engaged in foreign transportation and in competition with foreign air lines, must be given every advantage and opportunity to compete on the same level and under the same conditions with foreign air lines or else the efforts of the United States lines to engage in foreign transportation would be effectively thwarted. These are the reasons why the Board has maintained that "The vast extent of our future international air transportation operations and their economic and political significance is of great importance."⁸

In recent years a number of domestic carriers have entered the international field. These carriers are still in the early stages of development and experimentation. Energetic management and economic incentives are necessary if they are to meet the competition of foreign flag carriers. If, as contended by the Postmaster General, the domestic service of a United States carrier is to be burdened with the losses of its international service, the natural tendency would be to discontinue entirely or seriously curtail foreign service. Such a policy would deter other domestic carriers from even entering the foreign field. This fact was undoubtedly present in the mind of the Board when it concluded that the best interests of the United States would be served by not offsetting the earnings from C&S' domestic operation against "the 'need' resulting from the carrier's international routes."

⁸ *Northeast Air, et al., North Atlantic Routes*, 6 CAB 319, 325.

Aside from practical policy considerations designed to establish, encourage and promote foreign air transportation, it cannot be questioned that the Board's action in refusing to burden the domestic operation of C&S with its foreign operations is a proper and valid exercise of its general regulatory authority under the Act.

III.

THE BOARD HAS NO AUTHORITY TO OFFSET EARNINGS OF DOMESTIC DIVISION ARISING UNDER UNCHALLENGED FINAL RATES AGAINST THE NEED OF THE INTERNATIONAL DIVISION.

The Board, in its "Statement of Tentative Findings and Conclusions" (J. A. 21), based its decision not to offset any part of the earnings of the domestic division arising under unchallenged final rates against the need of the international division solely on reasons of economic policy. Although the Board, in its final opinion of October 18, 1951 (J. A. 55), specifically stated that it was not deciding the question of its legal power to make such an offset, we submit *that the Board had no statutory authority to make the offset* urged by the Postmaster General in the instant case.

The future rates established for the domestic division and applicable to the period beginning January 1, 1948, were *final* rates which were never challenged and are not now in issue. Since these permanent rates remained unchallenged,⁹ the Board is not empowered under the Act to retroactively revise such rates or to disturb past earnings arising thereunder by offsetting any part of the earnings earned under such rates.¹⁰ The offset of these earnings would, in effect, be a retroactive reduction of the final mail

⁹ On October 1, 1951 the Board (Order Serial No. E-5747) entered an order reopening the current final mail rates for the domestic operations of C&S and six other domestic trunk line carriers. On July 21, 1952 the Board (Order Serial No. E-6616) entered an order reopening the current final mail rate for the operations of C&S over its Latin American route.

¹⁰ *Transcontinental & Western Air, Inc. vs. CAB*, 169 F. 2d 893, 895, affirmed 336 U. S. 601 (1949), 93 L. Ed. 911.

rate for the domestic division. On this basis, the proposed offset would be plainly outside of the scope of the Board's jurisdiction as defined in the TWA case.¹¹

One of the most important of the statutory objectives, with which the Board is concerned, is to place carriers on permanent rates as rapidly as possible. The Postmaster General's reading of Section 406(b) would in effect preclude the Board from fixing a final rate for the domestic division of the carrier, would frustrate the statutory objective and would not harmonize with the clear purpose of the Act. Once having fixed a *final* rate for the domestic division alone, thereby segregating it as a rate-making entity, the Board cannot *retroactively* invalidate that rate by treating the domestic division as part of a new rate entity—the system—rather than an entity in and of itself.

If the Board had authority to make rates retroactive to any point of time, it would also have authority to offset past earnings as urged by the Postmaster General. But the Supreme Court has held in the TWA case¹² that the Board does not have the power to fix a new mail rate and to make it retroactive for a period in which a final rate previously fixed by the Board was in effect and unchallenged by the initiation of a mail rate proceeding. The Board and the Postmaster General have the power to institute a proceeding looking toward decrease of the rate for the domestic division when it passes the bounds of reasonableness. This the Postmaster General failed to do during 1948-1950, the period of higher earnings. If the Board had thought the domestic rate too high it should have reopened the domestic case, and if the Postmaster General felt the domestic rate too high, he should have requested the Board to reopen the case. The Board should not now be required to use indirect methods to accomplish that which it failed to do by direct and available legal means. Not having the power to make rates retroactive

¹¹ Idem.

¹² Idem.

to any point of time, it necessarily follows that the Board lacks the power at a future date to offset past domestic earnings under a final rate.

It is firmly established law that a public utility rate deals only with the future. It is not concerned with reimbursements of past losses nor with recapture of past profits. The first sentence of Sec. 406(a) simply empowers and directs the Board to fix rates. In no other public utility statute has such language been construed to contemplate a retroactive rate-making authority. There is nothing in the legislative history of the Civil Aeronautics Act of 1938 to indicate an intention or understanding that the Act contemplated a retroactive rate-making authority. The Board has held that under the Act in fixing a rate for the future it cannot capitalize past losses.¹³

It is well established that a regulated utility cannot be required to give up excess earnings from past operations.¹⁴ To subject to recapture earnings of air carriers in excess of a fair and reasonable rate would tend to sap management of those very incentives that are, in a private economy, essential if we would strive for efficiency. Sound administration of the Act not only requires no retroactive authority but can best be achieved without it. This conclusion is consistent with the Board's administration of the Act since its enactment in 1938.

The Board lacks the power to take such retroactive action unless Congress has plainly specified such power.¹⁵ The language of the Act does not suggest that Congress intended to break with the traditions of rate-making. There is no reference in the statute to an offset of past earnings or to a diminution of past profits. We think that if Congress intended to provide for the recapture of past

¹³ *Pennsylvania Central Airlines Corp., et al., Motions, supra.* See also *Galveston Elec. Co. v. Galveston*, 258 U. S. 388, 66 L. Ed. 678, and *Georgia Ry. v. E. E. Comm.*, 278 F. 242, aff. 262 U. S. 625, 67 L. Ed. 1144.

¹⁴ *Board of Commissioners vs. N. Y. Tel. Co.*, 271 U. S. 23, 70 L. Ed. 808. *Newton vs. Consolidated Gas Co.*, 258 U. S. 165, 66 L. Ed. 538.

¹⁵ *Neild vs. District of Columbia* (1940) 71 App. D. C. 306, 314, et seq., 110 F. 2d 246, 254, et seq.

profits through the process of offset, it would have spelled out the terms of the proposal in clear and unmistakable terms and would not have employed the phrases "shall take into consideration", "among other factors", and "all other revenue" which, if interpreted as now urged by the Postmaster General, would have a disastrous effect on the objectives of the Act. In view of the finality of the domestic rates, which stood unchallenged for more than three years, the Board is without power to offset the higher earnings of C&S' domestic division against the need of its international division.

IV.

THE BOARD IS NOT REQUIRED, UNDER SECTION 406(b) OF THE ACT, TO OFFSET EARNINGS FROM DOMESTIC OPERATIONS AGAINST THE "NEED" RESULTING FROM INTERNATIONAL OPERATIONS IN ESTABLISHING RATES APPLICABLE TO INTERNATIONAL OPERATIONS.

Assuming, *arguendo*, that the Board is legally empowered to offset earnings of the domestic division gained under a final rate in establishing proper rates for the international division, such power is discretionary rather than mandatory. The Postmaster General, however, contends that the Act *requires* the Board, in fixing the fair and reasonable rate of compensation to offset "all other revenue" of the carrier in determining the carrier's need. On the other hand, the Board and the carrier contend that while the Board is required by Sec. 406(b) *to take into consideration* the need of the carrier for mail compensation, together with "all other revenue", it is *not required to reduce* the carrier's mail pay with any part of such other revenue if there are sound reasons for not doing so as a matter of economic policy.

The Petitioner argues in his brief (page 14) that a carrier is to receive only such mail pay as it "needs" and

that such "need" is to be determined by *offsetting* "all other revenue" of the carrier. While Petitioner admits that it is the duty of the Board to fix mail rates in an amount which will provide the carrier with funds necessary to carry out the national air transportation policy, he denies the right of the Board to exercise any discretion in determining how much or how little in the way of mail pay is necessary to carry out the national air transportation policy. He contends that the duty of the Board *to consider* "all other revenue" means that the Board has no choice other than *to offset* "all other revenue". He further contends that the term "all other revenue" leaves no discretionary power in the Board to disregard a portion of such other revenue even if such act is justified by economic policy considerations and is necessary to carry out the national air transportation policy. Finally, Petitioner contends that the *source* of the carrier's "all other revenue" is immaterial and that the Board has no power, discretionary or otherwise, to disregard any portion of such other revenue, although "such other revenue" may have come either from non-carrier property or from a different class of service, as contemplated by the Act, and even though the national air transportation policy would be served best by disregarding a portion of the carrier's other revenue as the Board, in the exercise of its conferred discretion, did in the instant case. The limited and restrictive interpretation of the Act urged by Petitioner is so untenable that it would defeat the very purpose and scheme of the Act. We think that anyone reading the whole of the statutory provisions relative to the Board's authority to fix rates, and the various rate-making elements to be considered in fixing and determining fair and reasonable rates of compensation must conclude that the Board's interpretation of the Act is in harmony with the obvious design of the Act as set forth in Section 2 and Section 406(b).

A. The Meaning and Scope of Section 406(b) of the Act.

Section 406(a) of the Act directs the Board to fix "fair and reasonable" rates of compensation for the transportation of mail by aircraft. Section 406(b) of the Act provides that in determining the rate *in each case* the Board "shall take into consideration, among other factors"—

(1) the condition that the carrier holds and operates under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service;

(2) the standards respecting the character and quality of service to be rendered; and

(3) the need of each carrier for compensation sufficient to insure the performance of mail service.

The statute further provides that, in addition to the need of the carrier for compensation to insure the performance of mail service, the Board "shall take into consideration" a fourth factor, i.e., the need of the carrier for compensation to enable it "to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service and the national defense".

Congress fully recognized that there were "other factors" besides those above enumerated which the Board should consider in determining the rate in each case. Some of these "other factors" are set forth in the first sentence of Section 406(b), and include (1) conditions peculiar to transportation by aircraft; (2) conditions peculiar to the particular air carrier; and (3) conditions peculiar to a class of air carriers.

In addition to those factors enumerated in Section 406(b) there are other factors which Congress expressly directed the Board to consider "as being in the public interest and

in accordance with the public convenience and necessity". These other factors are contained in Section 2 of the Act (Appendix).¹⁶

The Postmaster General admits in his brief, (page 8), that the factor of "need" is not the only factor to be considered by the Board, but contends that this single factor is mandatory in the sense that the Board cannot award mail pay in an amount in excess of what the carrier needs. In the first place, there is nothing in the Act which picks out the need factor from all the other factors above enumerated and says that this one factor is a mandatory limiting feature. It is no more mandatory or limiting than any of the other factors. It is only to be taken into consideration with all the other factors, and the weight to be given to it rests in the experienced judgment and broad discretion of the Board. In the second place, Congress, in Section 2 of the Act, only directed the Board to "consider" certain special factors, and in Section 406(b) only directed that the Board "shall take into consideration" certain other special factors. Both sections of the Act give leave to the Board to consider customary rate-making factors not mentioned in either section. In Section 2 Congress used the phrase "among other things" and in Section 406(b) Congress used the phrase "among other factors". Congress rightfully left to the Board the power to determine what other factors and things should be considered, as well as what weight should be given to each factor, in furthering the public interest, convenience and necessity. The Board must weigh all the criteria found in the Act which gives substance and vitality to Congressional mandate of policy set forth in Section 2 of the Act. These widely ranged factors were considered by the Board in this case.

¹⁶ In *American Airlines vs. Civil Aeronautics Board*, 192 F. 2nd, 417, 420 (1951) this Court said "Whatever belittling significance may be attached to the fact that those provisions (Section 2) were under a title 'Declaration of Policy', they are in the statute, are peremptory, and are as much an enactment by the Congress as is any other section of the statute."

The *carrier's* need was only one of many factors for the Board to consider, and that factor obviously was not a mandatory or limiting one. A statutory provision directing an administrative agency to *consider* a particular factor *among other things or factors* is certainly not the equivalent of an express command to adopt a uniform course of action. Congress never intended or contemplated that the Board would or could adopt a uniform course of action that would fit all carriers or classes of carriers or classes of service. This becomes apparent in view of the very first sentence of Section 406(b) which provides that the Board shall consider the conditions peculiar to the particular air carrier or class of air carrier. By giving the Board the authority to fix different rates for different air carriers or class of air carriers and different classes of service, Congress recognized the practical impossibility of prescribing or of directing the Board to adopt a uniform course of action.

The Postmaster General further argues that the intent of Congress reflected in Section 406(b) of the Act is that the carrier is to receive only such mail rate as it needs, and that such need is to be determined by offsetting *all* and not some part of its other revenue.¹⁷ This argument is patently absurd, in view of the Postmaster General's admission that the Board has the power administratively to fix rates separately for different operating divisions of a carrier, as the Board has done in the instant case with respect to the domestic and international divisions of C&S. If the Board is *required* to offset *all* of the carrier's other revenue in determining the need of the international division, it must, in the instant case, offset *all* of the revenue of the domestic division and not a part of such revenue. The Board's position that it is only required to *consider* all of the carrier's other revenue is both reasonable and logical.

¹⁷ Petitioner's Brief, page 14.

There is nothing in the Act to support the Postmaster General's view that the source of the carrier's "all other revenue" is immaterial and that "all other revenue" must be offset in determining a carrier's mail rate need. Such view would not only penalize the efficient carrier and put a premium on inefficiency, but would also lead to such an absurd result that few would be hardy enough to venture into the field of foreign air transportation. For example, assuming, *arguendo*, that the Ford Motor Company operated an international route with a mail pay need clearly established at \$5,000,000 a year, and the company earned \$10,000,000 a year in its automobile manufacturing and sales. Under the Postmaster General's theory the Board would be required to offset all of the revenues of the automobile division against the need of the airline operations and as a result the airline operations would only be entitled to compensatory mail pay. What incentive would there be for the company to engage in the airline operation? What incentive would there be in the instant case for C&S to engage in foreign air transportation or in developing an economically profitable sound and efficient domestic operation?

It is fairly apparent that the Postmaster General's construction of the "all other revenue" clause in Section 406(b) would inevitably defeat the statutory objectives of the Act as defined in Section 2.

The only requirement in the Act is that the Board *consider* all other revenue. This the Board has done. It has not ignored the carrier's earnings from its domestic division in determining the need of its international division. It fully considered the need of the carrier for mail compensation, together with "all other revenue", and after weighing all factors concluded that there were sound reasons for not reducing the carrier's mail rate with any part of such other revenue as a matter of economic policy (J. A. 54).

B. The Need Factor.

The Postmaster General contends that the Board's construction of the Act would give the carrier a subsidy in excess of its actual need. The problem, of course, is to determine what is the carrier's actual need. According to the Postmaster General the Board should fix the need rate at a level to provide the carrier with sufficient income to (1) meet its entire operating charges; (2) pay its taxes; and (3) earn a fair rate of return on its invested capital. In other words, the Board should be limited to maintaining the carrier as an efficient going concern, and any payments in excess of the minimum amount required to insure the bare performance of mail service is in excess of the carrier's actual need and therefore is not authorized by the statute. The question is whether the Board is empowered by Section 406(b) to fix need mail rates which provide an allowance for incentive, developmental and other purposes in excess of that necessary to sustain an existing operation.

The Board is clearly empowered to do so. Section 406(b) does not limit the fair and reasonable rate to the minimum amount necessary to maintain an existing operation, nor is the statutory concept of "need" so limited. On the contrary, the term "need" as employed in Section 406(b), expressly includes not only the mail rate necessary to "maintain" a given operation, but also the mail rate necessary to "continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service and the national defense". The extent of a carrier's need is the extent of mail rate actually required to accomplish these developmental objectives. The powers conferred in administering the mail pay provisions of the Act obviously were designed and intended to be coextensive with the over-all policy responsibilities placed upon the Board. Due regard for the developmental directions contained in the Act has been recognized by the Court to

be "peremptory" upon the Board in certificate cases,¹⁸ and should be recognized as being equally peremptory in mail rate cases.

The Board has always considered that it has statutory authority to allow a mail rate in excess of minimum operating need for incentive and developmental purposes. The entire purpose of "need" payments is not simply to make a carrier financially whole, but to develop an air transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service and of the national defense. The Board's decision not to reduce the carrier's international mail pay with any part of its domestic earnings was not based on whether offsetting the domestic profits would or would not deny C&S a fair rate of return on each of its divisions, but was based on sound reasons of economic policy. If the Board, in the administration of the Act, is to accomplish the stated objectives for which it alone was created, it must be concerned not only with the costs of operation and a fair return on capital, but also with establishing incentives to operate efficiently, with resulting benefits to the public and eventual self-sufficiency to the end that the financial aid given will bring about, at the earliest possible time, the kind of air transportation system contemplated by the Act. To accomplish this may require in a particular case, as here, the inclusion of compensation in the rate for incentive and developmental purposes. The meaning which the Postmaster General seeks to have fastened on the word "need" is to limit such need merely to provide the carrier with sufficient income to maintain it as a going concern. This, conceivably, could be done in the instant case by adopting the offset policy and using the profits from the carrier's domestic operation to sustain its international operation, but, by doing so, it would destroy the carrier's incentive to improve and develop its air transportation system. The basic underlying

¹⁸ *American Airlines vs. Civil Aeronautics Board, supra.*

question is simply—does the Act confer discretionary power on the Board to determine the need of this particular air carrier?

C. The Act Confers Discretionary Powers on the Board to Exclude "Other Revenue" Where Such Action Effectuates Statutory Policy.

One of the basic objectives of the Act is to foster and develop a greater degree of operating efficiency in the industry, with a view to ultimate self-sufficiency.¹⁹

The duty of developing the air transportation system rests upon the Board and not upon the Postmaster General, and the Board's judgment as to the need of the particular air carrier should be conclusive.

The Postmaster General contends that the Board lacks discretionary power to find that the earnings from C&S' domestic routes should not be used to offset the "need" resulting from the carrier's international routes, even though the Act does authorize the Board to fix rates separately for the different operating divisions of the carrier.

Section 406(b) of the Act clearly vests in the Board the duty to consider all possible and pertinent factors, including the factor of the carrier's need, and equally clearly vests in the Board the discretion to exclude "other revenue", if such action will best effectuate the statutory policy. The Board has, on many occasions, stated its position that the "all other revenue" clause of Section 406(b) affords it discretion with regard to the propriety of recognizing such items for the purpose of reducing "need" in final rate proceedings.

The provisions of Section 406(b) plainly indicate that the determination of "the need of each such carrier" involves the exercise of sound administrative judgment.²⁰ The basic purpose of the need clause of Section 406(b)

¹⁹ *Pennsylvania Central Airlines, et al., Motions*, 8 C. A. B. 685, 696-697 (1947).

²⁰ *Pan American Airways Co. (Del.), Transatlantic Mail Rates*, 1 CAB 220, 253 (1939); *American Airlines, Inc., Mail Rates*, 3 CAB 323, 336 (1942).

is to assist in the development of the air transportation system of the United States. Accordingly, it is self-evident that in cases where reduction of the "need" of the carrier's international division, by offset of earnings of the domestic division, would not in the judgment of the Board serve to foster and develop the air transportation system contemplated by the Act, the Board in its discretion may properly refuse to make such offset. Even if the Court disagreed with the Board on that proposition, the Board's decision would not necessarily be invalid because there would remain the exercise by the Board of the discretion plainly conferred upon it by Section 2 of the Act.

The Postmaster General's construction of the Act would leave no room for discretion and would require the Board to "offset" earnings of the domestic division in determining the rate for the international division in complete disregard of other special and traditional rate-making factors and the stated objectives of the Act. The word "offset" does not appear in Section 406(b) of the Act. The Postmaster General's construction that "offset" is required cannot reasonably be inferred from the express statutory language that the Board "shall take into consideration, among other factors," . . .

V.

THE BOARD'S INTERPRETATION OF SECTION 406(b) OF THE ACT IS REASONABLE AND PROPER.

The Board, in its "Statement of Tentative Findings and Conclusions" (J. A. 19), stated that it had considered the possible offset of a portion of the revenues realized by C&S under its domestic mail rate against the need which would otherwise be found to exist in relation to C&S' international operation, with a resulting reduction in the mail pay to be provided for such operation, but it found that policy considerations rendered such offset inappropriate in this case. In its final opinion (J. A. 54) the

Board reaffirmed its earlier view and concluded that, *as a matter of economic policy*, sound reasons existed for finding that the earnings from C&S' domestic routes should not be used to offset the "need" resulting from the carrier's international routes. The refusal of the Board to make the proposed offset was based on its interpretation of Section 406(b) together with the other provisions of the Act, particularly Section 2 thereof. The Board properly concluded that the offset policy proposed by the Postmaster General in the instant case was not in the public interest. The conclusion not to recapture past earnings over a substantial period of time was in line with established Board policy.

The Board on numerous occasions has determined that considerations of economic policy under the Act render it inconsistent with the public interest to affect retroactively rates for air mail compensation so as to require refund to the Government of moneys paid over an extensive period of time. To this effect, in *Pan-American Grace Airways, Mail Rates*,²¹ the Board held:

"Other considerations have been advanced against the adoption of a policy which would involve the recapture of past earnings accumulated over a substantial period of time. Without doubt, even under the most favorable circumstances, the policy would impede long-range planning and would inject a measure of uncertainty into undertakings looking toward the expansion and development contemplated by the Civil Aeronautics Act. It would in all likelihood reduce managerial incentive to accomplish increased economies in operation. Management could hardly be expected to exert itself energetically to such purpose with the ever-present fear, however unfounded it might be, that money saved through increased economies would be taken away. * * *"

Accordingly, the Pan American-Grace earnings held by the Board to be excessive were not recaptured. This same

²¹ 3 CAB 550, 564-565 (1942).

policy has been consistently maintained in a series of subsequent rate cases both domestic and international.²²

We have previously stated that one of the primary objectives of the Act is to further the development of the air transportation industry to a point where it will attain a self-sufficient status. Unquestionably, this goal is best obtainable by placing carriers on permanent rates rather than on a cost-plus basis for mail payments.²³ It is only under permanent rates that a carrier has the incentive to operate efficiently on the theory that it may retain any profits it earns in excess of the estimated return to be afforded by its mail rate.

In fixing the final domestic rate in the 1948 *C&S Domestic Mail Rate Case*,²⁴ the Board in commenting upon the estimated rate of 7.4% stated:

“ * * any economies which the carrier's management succeeds in accomplishing through affective cost controls or improved operating procedures and techniques, which served to avert or mitigate anticipated increases in prices and to decrease operating costs below the unit cost of 116.6 cents per revenue plane mile estimated herein, will insure to the carrier in the form of higher earnings.”* (Emphasis Supplied).

In other words, the Board specifically held that a 7.4% return was not to be considered a ceiling, and encouraged the carrier's management to increase the rate of return through progressive management policies.

The Postmaster General was a participant in the above proceeding but took no exception to the Board's findings and policy above quoted, although the C&S international division was on a temporary rate basis at the time. The Board's holding in the 1948 domestic case was no more nor less than an undertaking (joined in by the Postmaster

²² *Pan-American Airways, Inc., et al., Latin American Rate Case*, 3 CAB 657 (1942); *Eastern Air Lines, Inc. Mail Rate Proceeding*, 3 CAB 733 (1942); *American Air Lines, Inc. Mail Rate Proceeding*, 3 CAB 770 (1942).

²³ *Transcontinental & Western Air, Inc. vs. C. A. B.*, *supra*.

²⁴ 9 CAB 786, 812 (1948).

General through acquiescence) not to recapture domestic earnings in excess of 7.4%. The Postmaster General took no steps to review C&S' domestic rate as he could have done through appropriate legal action, and therefore as a matter of equity and fair play he should not now be heard on his contention that the higher domestic earnings should be recaptured in the international rate.

The adoption of a policy of offsetting profits of a domestic division *earned under a final rate* against the need of the carrier's international division would constitute a real deterrent to operating economy and efficiency. The Board has also recognized that, as a practical matter, if past domestic earnings are to be taken from a carrier to offset the need of its international division, there would be no incentive to live within the domestic rate. Instead of the carrier becoming self-sufficient over a period of time, as is the case under the Board's present policy, it would become increasingly more dependent upon a mail pay subsidy and never reach the goal of self-sufficiency.

The Board has frequently recognized its responsibility to place carriers under permanent rates. The Board's experience has shown that, as a practical matter, unless a permanent rate can be fixed for domestic operations without the necessity for determining simultaneously the rate for international division, it may often prove to be impossible to fix any permanent rate for any division for an extended period of time. We submit that adoption of the offset policy would deprive the Board of the power to fix *final* future rates on a divisional basis. In practical effect, any carrier with one or more divisions of its system operating on a temporary rate will be operating its entire system on temporary rates until such indefinite future time as rates have been finalized for each and all of the operating divisions.

If the offset policy were adopted, thus permitting the Board, in effect, to recapture past earnings on domestic operations under permanent mail rate order, serious

financial confusion would follow. Such a policy would not only impede long-range planning, but would inject great uncertainty in any plan of the carrier to expand and develop, as no large commitment would be conclusively feasible. Such a policy would reduce incentive instead of rewarding efficiency. Such a policy would mislead investors and would impair the carrier's ability to attract capital, because no financial statement could correctly reflect the carrier's financial status, no dividend declaration would be secure, and no offering of securities would have a firm foundation.²⁵

Under the procedure urged by the Postmaster General profits would be confiscated retroactively after stockholders have been assured of earnings, dividends have been declared and paid, new equipment has been purchased and all company economic and financial policies have been formulated on the justifiable assumption that such profits were real.²⁶

The Board, in refusing to adopt the offset policy in the instant case, recognized the likelihood that the domestic and more robust segment of the industry would be unfairly burdened with the economically weaker international segment. The Board correctly reasoned that such course would be contrary to the public interest, for if the domestic segment was kept strong and financially sound, fare reductions would follow, more modern aircraft would be acquired, and safer and more efficient operations would result. It is obvious that if the carrier's domestic division now, at long last on the road to self-sufficiency, is to be burdened with the comparatively infant and far from self-sufficient international operation, the efficient and economical carrier would either refuse to continue in, or refuse to enter into, the present financially unprofitable for-

²⁵ *T. W. A. v. CAB, supra.*

²⁶ The permanent domestic mail rate of C&S was established and set with no indication either in the Opinion and Order (Order Serial No. E-1825, Docket Nos. 1335 and 1897, adopted July 28, 1948) or in the rate case conferences with the Board's staff that any profits made thereunder would be subject to recapture in the international rate case.

eign or international service. The inevitable result would be that the international field would be dominated by air carriers operating under foreign flags and the foreign commerce requirements, the Postal Service and the national defense of this country would suffer, contrary to the purposes and design of the Act. It is submitted that these considerations are of extreme importance to the maintenance and development of both domestic and foreign air service, and that the two types of service must be kept separate and apart if either are to thrive and maintain a competitive position in their respective fields.

The Board's policy in not offsetting domestic profits is desirable from a purely administrative standpoint, because in administering the Act it is highly desirable to maintain a comparative status between domestic operators which have foreign routes, as against those which do not have foreign routes. Maintaining such comparative status has enabled the Board to fix uniform domestic mail rates for groups of carriers. This would not be feasible or possible if the Board lacked the power to exclude from consideration the needs of international operations. If the Board were required to fix rates for both domestic and international operations at the same time, it would be practically impossible to find a suitable basis for a comparison technique of analysis. The Board's long experience has shown that the comparison technique of rate-making is the most desirable to follow.

The adoption of a policy of offsetting profits of a domestic division while in a final rate against the need of the carrier's international division would unfairly penalize the carrier especially in view of the fact that had domestic losses been suffered during this period they could not have been recovered by the carrier through its final international mail rate. While operating under a final rate, the carrier takes the risk of loss, without possibility of later reimbursement through mail pay and it is therefore only equitable that the carrier should retain the benefit of good earnings resulting from keen management.

In view of the foregoing arguments, we submit that the Board's interpretation of Section 406(b) of the Act is both reasonable and proper.

VI.

THE BOARD'S INTERPRETATION OF SECTION 406 (b), BEING PROPER AND REASONABLE, SHOULD BE BINDING UPON THE COURT ON A PETITION FOR REVIEW.

Since the parties have stipulated that no facts are in controversy, the primary question before this Court is one of law and is whether the Board's interpretation of Section 406(b) of the Act should be sustained.

The Board, in its well considered opinion of October 18, 1951, concluded that in fixing just and reasonable air mail rates for the Latin American routes of C&S, it was not required under Section 406(b) of the Act to offset past earnings from the carrier's domestic operations and decided "for reasons of economic policy" that the rates to be prescribed for the carrier's international routes should not be reduced by any amount of the earnings from its domestic operations. As has been previously discussed, there is warrant in the record and a reasonable basis in law for the Board's interpretation of the statute.

It is a well settled principle, supported by numerous decisions, that the Court should give great weight to the construction placed upon a statute by an administrative agency charged with the responsibility for the administration and enforcement of the statute. In *Brooks Transp. Co. v. United States*, 93 F. Supp. 517, affirmed 340 U. S. 325, 95 L. ed. 668, the Court said, "Though the question here involved is one of law, it is well settled that the courts should give great weight to the Commission's interpretation of the Act." As Mr. Justice Burton stated in his opinion in *Levinson v. Spector Motor Co.*, 330 U. S. 649, 672, 91 L. ed. 1158, "in the light of the Commission's long

record of practical experience with this subject and its responsibility for the administration and enforcement of this law, the conclusions (of the Commission) are entitled to special consideration." See also *United States v. American Trucking Associations*, 310 U. S. 534, 549, 84 L. ed. 1345; *Colgate Palmolive Peet Co. v. United States*, 320 U. S. 422, 426, 88 L. ed. 143; *McLean Trucking Co. v. United States*, 321 U. S. 67, 87-89, 88 L. ed. 544.

The national air transportation policy, as provided for under Section 2 of the Act, expressly requires the Board to consider, among other things, the encouragement and development of an air transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States; the regulation of air transportation in such a manner as to recognize and preserve the inherent advantages of, and foster sound economic conditions in, such transportation; the formation of adequate, economical, and efficient service by air carriers at reasonable charges; competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense; the regulation of air commerce in such manner as to best promote its development and safety; and the encouragement and development of civil aeronautics. Resolving these considerations, in determining whether air mail rates for international routes will effectuate the overall air transportation policy, is a complex task which requires extensive facilities, expert judgment and considerable knowledge of this form of transportation. Congress has left this task to the Civil Aeronautics Board. The experience and the wisdom of the Board, not of the Court, or of the Postmaster General, must determine the question of reasonable and proper rates. As Mr. Justice Rutledge said in *McLean Trucking Company v. United States*, 321 U. S. 67, 88, 88 L. ed. 544, 557, "If the Commission did not exceed the statutory limits within

which Congress confined its discretion and its findings are adequate and supported by evidence, it is not our function to upset its order."

In attaining the objectives of the national air transportation policy, it is the function of the Board to interpret the language used by Congress to carry out the legislative intent. The Board is trained for this purpose. Administrative interpretation of a statute carries persuasiveness as an expression of view of those experienced in the administration of the Act and acting with the advice of a staff specializing in its interpretation and application. *Overnight Motor Transp. Co. v. Missel*, 316 U. S. 572, 86 L. ed. 1682. Administrative agencies designated by Congress as specialists in a particular field and advised by experts are in a better position than a reviewing Court to determine appropriate applications of statutes which they are directed to administer. *National Labor Relations Board v. Medo Photo Supply Corporation*, 135 F. 2d 279, affirmed 321 U. S. 678, 88 L. ed. 1007.

To sustain the Board's interpretation of Section 406(b) the Court need not find that the Board's construction is the only reasonable one, or even that it is the result the Court would have reached had the question arisen in the first instance in judicial proceedings. The reviewing Court's function is limited. All that is needed to support the Board's interpretation is that it has a warrant in the record and a reasonable basis in law. *Unemployment Compensation Commission v. Aragon*, 329 U. S. 143, 153, 154, 91 L. ed. 136, 145, citing *National Labor Relations Board v. Hearst Publications*, 322 U. S. 111, 88 L. ed. 1170, and *Rochester Telephone Corp. v. United States*, 307 U. S. 125, 83 L. ed. 1147.

In *American Airlines v. Civil Aeronautics Board*, (7th Cir. 1949), 178 F. 2d 903, the petitioners sought to review an order of the Board authorizing air freight forwarders to engage indirectly in interstate air transportation. Petitioners contended that the Board's findings were insufficient

to sustain the order and that the Board erroneously interpreted the law. The Court found that there were sufficient findings upon which the Board based its order and sustained the interpretation the Board gave to Section 408(b) of the Act. The Court stated:

"Obviously, we are not concerned with the question of whether this was a wise course of action. Nor are we concerned with whether we would have entered the order ourselves or whether the board's interpretation is the only reasonable one. Our function is limited; we may only inquire as to whether the board's interpretation of the statute has warrant in the record and a reasonable basis in the law. *Unemployment Compensation Commission v. Aragon*, 329 U. S. 143, 153-154, 67 S. Ct. 245, 91 L. ed. 136. See also *National Labor Relations Board v. Hearst Publications*, 322 U. S. 111, 131, 64 S. Ct. 851, 88 L. ed. 1170.

"It would seem unnecessary to reiterate that presumptively the board's order is correct, and, under any and all circumstances, its decision is entitled to great weight. It is not for the federal courts to supplant the Commission's judgment even in the face of convincing proof that a different result would have been better."

In concluding, the Court said:

"We think that the interpretation of the statute by the board in order to avoid incongruous result and in order to effectuate the intent of Congress was proper under *United States v. American Trucking Ass'ns*, 310 U. S. 534, at 542-544, 60 S. Ct. 1059, 84 L. ed. 1345 and authorities there cited. To the same effect is the recent decision of the Court of Appeals for the Second Circuit in *North American Utility Securities Corp. v. Posen, et al.*, 1949, 176 F. 2d 194. We conclude that the board's interpretation of the second provision of Section 408(b), which makes it inapplicable to the acquisition of control of an air freight forwarder, carries out the intent of Congress and is a reasonable and proper interpretation of that provision binding upon this court. *National Labor Relations Board v. Hearst Publications*, 322 U. S. 111, 130, 64 S. Ct. 851, 88 L. ed. 1170; *Unemployment Compensation Commission v. Aragon*, 329 U. S. 143, 153-154, 67 S. Ct. 245, 91 L. ed. 136."

In the case of *United States v. American Trucking Association*, 310 U. S. 534, 549, 84 L. ed. 1345, the question raised on review was as to the meaning of Section 240(a) of the Motor Carrier Act of 1935. The Supreme Court upheld the construction given to the statute by the Interstate Commerce Commission and stated that administrative interpretations of a statute are entitled to great weight where they involve a contemporaneous construction of the statute by the persons charged with the responsibility of setting its machinery in motion and of making its parts work efficiently and smoothly.

In *National Labor Relations Board v. Denver Bldg. & Const. Council*, 341 U. S. 675, 95 L. ed. 1284, the Supreme Court upheld an order of the National Labor Relations Board and reversed a judgment of the United States Court of Appeals for the District of Columbia refusing to enforce the Board's order which enjoined a labor organization from engaging in a strike. The Court accepted the holding of the Board that the strike was an unfair labor practice within the meaning of section 8(b)(4)(A) of the National Labor Relations Act. The Court stated:

"Not only are the findings of the Board conclusive with respect to questions of fact in this field when supported by substantial evidence on the record as a whole, but the Board's interpretation of the Act and the Board's application of it in doubtful situations are entitled to weight."

Among numerous other decisions which have held that Courts must give great weight to an administrative agency's interpretation of its governing statute are *West Texas Utilities Co. v. NLRB*, 184 F. 2d 233, 87 U. S. App. D. C. 179, certiorari denied 341 U. S. 939, 95 L. ed. 1366; *Billings v. Truesdell*, 321 U. S. 542, 88 L. ed. 917; *Augustus v. Commissioner of Internal Revenue*, 118 F. 2d 38, certiorari denied 313 U. S. 585, 85 L. ed. 1540; *Bowles v. Mannie & Co.*, 155 F. 2d 129, certiorari denied 329 U. S. 736, 91 L. ed. 636; *Railroad Retirement Board v. Duquesne Warehouse Co.*,

149 F. 2d 507, 80 U. S. App. D. C. 119, affirmed 326 U. S. 446, 90 L. ed. 192.

In its "Statement of Tentative Findings and Conclusions" adopted May 18, 1951, and in its decision of October 18, 1951, the Board applied the principle that while it is required to take into consideration the need of a carrier for mail compensation, together with "all other revenue," it is not required by Section 406(b) to reduce the carrier's mail pay with any part of such other revenue if there are sound reasons for not doing so as a matter of economic policy (J. A. 54). We see nothing in the Board's view to require the Court to substitute a different construction of Section 406(b) from that made by the Board which is entrusted with the responsibility of administering it and the duty of effectuating the declared policy and purposes of the Act.

The construction urged by the Board of Section 406(b) is consistent with the language of that section and with the policy of the Civil Aeronautics Act with respect to the encouragement, development and regulation of air transportation required for the commerce of the United States, the Postal Service and the national defense. The Postmaster General's construction runs counter to the declared policy of the Act and in view of the express language of Section 406(b), is unwarranted.

The Board, not the Postmaster General, is charged with the administration of the Act for the purposes and policies declared in the Act. The Board, a skilled and experienced body, is entrusted with the responsibility of initially applying the statutory provisions to the facts of each particular case. Its interpretation that it was not required under Section 406(b) of the Act to offset excess past earnings of the carrier in its domestic operations in fixing mail rate for the carrier's Latin American operations is supported by the record and has a reasonable basis in law. As a matter of law, the Board's interpretation should be accepted by this Court and the Board's decision of October 18, 1951 should be sustained.

CONCLUSION.

The regulatory function of the Board, insofar as it includes authority to fix rates for transportation of air mail, is a forward looking function. In that respect it differs from a purely judicial determination of present or past rights. When a regulatory action contemplates a new mail rate a type of judgment is required which is wholly absent from the mere valuation of past facts. In fixing and determining fair and reasonable rates of compensation under Section 406 of the Act, the Board must resolve the issue of public interest, convenience and necessity, not only upon the basis of insuring the performance of mail transportation service, but by also taking into account and giving appropriate weight to broad considerations of future welfare related to the development of the air transportation industry. The Board has well said that such an approach "must necessarily be predicated upon future estimates as well as present facts, for it is keyed to future goals and an effort to envisage the shape of things to come".

The Board, in fixing air mail rates for the Latin American operations of C & S, under its order of October 18, 1951, based its judgment on available facts as to present operations, business practices and past experience with air transportation operations. It also took into account and gave appropriate weight to the future welfare of the carrier and the development, encouragement and promotion of air transportation in accordance with the declared policy of the Act. In prescribing the rates which it considered to be consistent with the public interest, the Board did not exceed the statutory limits within which Congress confined its discretion. Its findings are supported by the evidence and comply with the requirements of the Act.

In the light of the Board's practical experience with air transportation, the Court should follow the interpretation of the statute given by the Board, the agency to which Congress has given the duty and imposed the obligation of administering the Act.

Upon the basis of the foregoing reasons and authorities,
the Board's order of October 18, 1951 should be affirmed.

Respectfully submitted,

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Dated: September 26, 1952.

APPENDIX.

The Civil Aeronautics Act of 1938, 52 Stat. 977, as amended, 49 U. S. C. 401, *et seq.*, provides in pertinent part as follows:

"DECLARATION OF POLICY

"Sec. 2. In the exercise and performance of its powers and duties under this Act, the Authority shall consider the following, among other things, as being in the public interest, and in accordance with the public convenience and necessity—

(a) The encouragement and development of an air-transportation system properly adapted to the present and future needs of the foreign and domestic commerce of the United States, of the Postal Service and of the national defense;

(b) The regulation of air transportation in such manner as to recognize and preserve the inherent advantages of, assure the highest degree of safety in, and foster sound economic conditions in, such transportation, and to improve the relations between, and coordinate transportation by air carriers;

(c) The promotion of adequate, economical, and efficient service by air carriers at reasonable charges, without unjust discriminations, undue preferences or advantages, or unfair or destructive competitive practices;

(d) Competition to the extent necessary to assure the sound development of an air-transportation system properly adapted to the needs of the foreign and domestic commerce of the United States, of the Postal Service, and of the national defense;

(e) The regulation of air commerce in such manner as to best promote its development and safety; and

(f) The encouragement and development of civil aeronautics." (49 U. S. C. 402)

"RATES FOR TRANSPORTATION OF MAIL

AUTHORITY TO FIX RATES

"SEC. 406. (a) The [Board] * * * is empowered and directed, upon its own initiative or upon petition of the Postmaster General or an air carrier, (1) to fix and determine from time to time, after notice and hearing, the fair and reasonable rates of compensation for the transportation of mail by aircraft, * * * and the

rates so fixed and determined shall be paid by the Postmaster General from appropriations for the transportation of mail by aircraft." [49 U. S. C. 486(a).]

"RATE-MAKING ELEMENTS

"SEC. 406. (b) In fixing and determining fair and reasonable rates of compensation under this section, the [Board] * * *, considering the conditions peculiar to transportation by aircraft and to the particular air carrier or class of air carriers, may fix different rates for different air carriers or classes of air carriers, and different classes of service. In determining the rate in each case, the [Board] * * * shall take into consideration, among other factors, the condition that such air carriers may hold and operate under certificates authorizing the carriage of mail only by providing necessary and adequate facilities and service for the transportation of mail; such standards respecting the character and quality of service to be rendered by air carriers as may be prescribed by or pursuant to law; and the need of each such air carrier for compensation for the transportation of mail sufficient to insure the performance of such service, and, together with all other revenue of the air carrier, to enable such air carrier under honest, economical, and efficient management, to maintain and continue the development of air transportation to the extent and of the character and quality required for the commerce of the United States, the Postal Service, and the national defense." [49 U. S. C. 486(b).]

"THE PRESIDENT OF THE UNITED STATES

"Sec. 801. The issuance, denial, transfer, amendment, cancellation, suspension, or revocation of, and the terms, conditions, and limitations contained in, any certificate authorizing an air carrier to engage in overseas or foreign air transportation, or air transportation between places in the same Territory or possession, or any permit issuable to any foreign air carrier under section 402, shall be subject to the approval of the President. Copies of all applications in respect of such certificates and permits shall be transmitted to the President by the Authority before hearing thereon, and all decisions thereon by the Authority shall be submitted to the President before publication thereof." (49 U. S. C. 601).